



AR07



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Corporate Profile

MacMillan Bloedel, Canada's largest forest products company, has integrated operations in Canada and the United States and other major operations and investments in the United Kingdom and Continental Europe.

The Company manages 1.6 million hectares of productive timberlands, which supply approximately 80 per cent of its total fibre requirements. Of these timberlands, 1.1 million hectares are in British Columbia, where the Company's headquarters and approximately 60 per cent of its assets are located.

The Company's products are marketed throughout the world and include lumber, panelboards, kraft pulp, newsprint, groundwood specialty papers, fine papers, containerboard and corrugated containers.

Annual Meeting

The Annual General Meeting of Common shareholders will be held in the ballroom of the Hyatt Regency Hotel, 655 Burrard Street, Vancouver, B.C., on Thursday, April 22, 1982 at 10 a.m.

Shareholders are invited to attend this meeting, take part in discussions about the Company and meet the directors and officers responsible for the operation of MacMillan Bloedel.

Highlights

Financial Results

	1981	(\$ millions)	1980
Sales and other income	2,230.1		2,456.2
Earnings (loss) before extraordinary item	(26.7)		113.2
Net earnings after extraordinary item	3.3		113.2
Cash flow from operations	32.8		245.9
Return on invested capital (Note 1)	.1 %		12.0%
Return on Common shareholders' equity (Note 3)	(1.5)%		14.3%

Per Common Share

		(\$ per Common share)
Earnings (loss) before extraordinary item (after preferred dividends)	(1.94)	5.03
Net earnings (loss) after extraordinary item (after preferred dividends)	(.53)	5.03
Cash flow from operations	1.54	11.56
Dividends	1.15	1.75
Book value (year end)	35.05	36.76

Assets

		(\$ millions)
Capital expenditures	307.9	327.7
Total assets (year end)	2,172.1	2,075.2
Invested capital (year end) (Note 2)	1,889.9	1,802.0

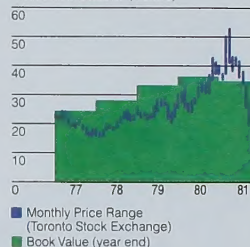
Additional Information

Debt as a percentage of invested capital (year end)	38.3%	35.0%
Common shareholders of record (year end)	10,269	14,017
Common shares outstanding (year end)	21,419,193	21,272,975
Number of employees (year end)	22,049	24,730
Wages, salaries and employee benefits (\$ millions)	683.7	688.4

Notes:

1. "Return on invested capital" is defined as net operating profit after taxes (NOPAT) as a percentage of average invested capital. NOPAT is defined as the sum of net earnings before extraordinary items and minority interests, the change in deferred income taxes, and interest expense net of associated current taxes.
2. "Invested capital" is defined as the sum of interest-bearing debt, deferred income taxes, minority interests, preferred share capital, and Common shareholders' equity including retained earnings.
3. "Return on Common shareholders' equity" is defined as net earnings available to Common shareholders as a percentage of average Common shareholders' equity.

Common Shares (\$/share)



Letter to shareholders

The 1981 numbers speak for themselves. A disastrous year! The principal reasons for such poor results were, as previously reported, extremely depressed markets for solid wood products, prolonged strikes at our mills and in the forest in British Columbia, and high interest costs.

I had hoped that by now signs of an economic recovery would be apparent, based on which I could report an improved outlook for the Company.

This is not the case, however, in the sense that no such signs are as yet apparent, but I nevertheless believe we will see seasonal improvement before too long and definite signs of general economic recovery before the end of 1982.

Meanwhile worldwide markets for solid wood products are still extremely weak. In our principal markets — the United States and Canada — the central banks appear

resolute in their intention to fight inflation with high interest rates for whatever length of time it takes to reverse inflationary expectations. Considering the lead time that builders require before they can resume activity once affordable mortgage money becomes available, it would appear that little improvement can be expected this year in North American housing production.

Concerns have been expressed that what is happening to the housing market in the United States and Canada is considerably more serious than the normal cyclical downturn of the type we have previously experienced. Some observers have advanced the view that deep-seated, long term structural changes are taking place as a result of current economic policies and changes in lifestyle. Some economic forecasters are suggesting fewer housing starts and smaller units than in the past, which would result in a long term lower demand for lumber and plywood.

On the other hand, it is not at all certain that the housing industry is undergoing anything more than a severe cyclical downturn. In past downturns, housing consumers,

particularly first-time buyers, have always lowered their sights on unit size and then either remodelled up or traded up as times got better. There is no factual information that I know of that would indicate that North Americans are likely to put a lower value on single family detached home ownership than they traditionally have in the past.

Whatever the long term trend might be, we expect a cyclical upturn in housing when mortgage rates back off to more reasonable levels. As in the past, sharply increased demand for lumber and panelboards will strain the limits of overall production capacity (which is currently being eroded as a result of the extended economic downturn) and prices will not only recover but probably escalate to new highs.

On the pulp and paper side, no fundamental changes appear to be confronting us and the long term outlook remains very favourable. Nevertheless the outlook for 1982 is discouraging in some respects.



There is a growing weakness in newsprint due to the current recession and the start-up of six large, new newsprint machines on the West Coast in 1981 and 1982 for a 40 percent increase in capacity. Operating rates for newsprint machines in Canada are now expected to be between 80 and 85 percent, which means we must anticipate the equivalent of up to six weeks' downtime at our newsprint mills this year.

Market pulp, containerboard and packaging are also adversely impacted by current recessionary conditions and some market-related downtime in those mills is also anticipated. Contrary to the newsprint situation, however, we expect shortages for these products in the next upturn because capacity expansions have not kept pace with the trendline of demand in recent years.

In light of all the foregoing, it is clear that present business risks and economic uncertainties are relatively high. In response to the squeeze on profits and cash flow, the Board felt it necessary last October to reduce the quarterly

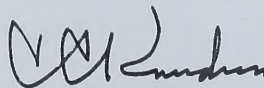
dividend to ten cents per share and no year-end extra dividend was declared at the end of 1981. In addition, the Company has now added to its already established program of restraint. Specifically, we have adopted and are implementing the following programs:

- a program of salary restraint for salaried employees, generally involving temporary salary reductions of 15 percent for upper salary levels and 10 percent for middle salary levels.
- a program of capital spending restraints aimed at reducing our capital spending from the budgeted level of \$240 million in 1982, which level in turn was down from \$308 million in 1981 and \$328 million in 1980.
- a program to streamline our British Columbia operational structure by converting from product line groups (Raw Materials, Building Materials, Pulp and Paper) to regional business units (Nanaimo Region,

Alberni Region, Powell River Region).

- a program of continued emphasis on the control and reduction of direct and indirect costs through increased efficiency and improved productivity at all levels.
- continuation of our program to liquidate or divest assets and businesses which are not expected to produce a satisfactory return on assets employed over the business cycle and do not otherwise serve an important strategic purpose.

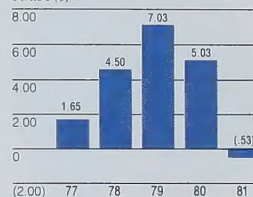
By responding to the current situation broadly on all fronts, we are confident that the Company will emerge from this recession financially strong and poised to gain the maximum possible benefit from the upcoming economic recovery.



C. C. Knudsen,
Chairman and
Chief Executive Officer

Vancouver, Canada
March 22, 1982

Net Earnings (Loss) per Common Share (\$)



Five Year Earnings Data



1981 Sales by Market

■ Canada
■ United States
■ United Kingdom and Europe
■ Japan and Orient
■ Other

Sales of products and services (\$ millions)	1977	1978	1979	1980*	1981
Raw materials and building materials	\$ 860.9	\$1,031.7	\$1,176.5	\$1,156.7	\$ 946.9
Pulp and paper	576.2	672.5	672.4	914.9	830.9
Containerboard and packaging	307.5	352.4	414.0	515.1	524.5
Other	41.3	27.0	32.5	29.6	33.2
	1,785.9	2,083.6	2,295.4	2,616.3	2,335.5
Less: Inter-segment eliminations	78.6	78.7	115.1	179.9	125.8
Total sales	\$1,707.3	\$2,004.9	\$2,180.3	\$2,436.4	\$2,209.7

Contributions to earnings (\$ millions)

Raw materials and building materials	\$ 29.4	\$ 92.1	\$ 155.4	\$ 56.9	\$ (82.2)
Pulp and paper	116.7	137.5	122.5	131.2	92.1
Containerboard and packaging	18.8	17.5	26.9	38.5	31.4
Other	(9.5)	1.9	1.4	1.1	.9
Less: Inter-segment eliminations	(1.2)	(3.0)	4.6	.1	(2.4)
Operating earnings	156.6	252.0	301.6	227.6	44.6
Corporate gains and losses	15.9	(11.7)	11.9	21.3	6.1
Investment income	3.7	8.2	10.3	5.1	15.6
Unallocated general and administrative expenses	(30.3)	(44.9)	(37.9)	(41.9)	(53.0)
Interest expense	(32.3)	(32.7)	(28.9)	(31.9)	(63.2)
Earnings before income taxes and undernoted items	113.6	170.9	257.0	180.2	(49.9)
Less: Income taxes	54.1	77.5	100.3	63.0	(31.3)
Earnings (loss) before undernoted items	59.5	93.4	156.7	117.2	(18.6)
Equity in earnings (losses) of partly-owned companies	3.2	9.4	1.8	—	(3.9)
Minority interests in subsidiaries	(2.0)	(1.9)	(3.6)	(4.0)	(4.2)
Earnings (loss) before extraordinary items	60.7	100.9	154.9	113.2	(26.7)
Extraordinary items	(22.3)	—	—	—	30.0
Net earnings	\$ 38.4	\$ 100.9	\$ 154.9	\$ 113.2	\$ 3.3
Less: Provision for preferred dividends	3.3	5.2	5.3	6.2	14.7
Net earnings (loss) available for Common shareholders	\$ 35.1	\$ 95.7	\$ 149.6	\$ 107.0	\$ (11.4)

Per Common share data (\$/Common share)

Operating earnings	\$ 7.37	\$ 11.85	\$ 14.18	\$ 10.70	\$ 2.09
Net earnings (loss) — before extraordinary item	2.70	4.50	7.03	5.03	(1.94)
— after extraordinary item	1.65	4.50	7.03	5.03	(.53)
Cash dividends	.40	.95	1.75	1.75	1.15

*Certain 1980 amounts have been reclassified

Results of Operations

Sales and Net Earnings

Over the past five years the Company's sales of products and services have shown a distinct upward trend; sales increased from \$1.71 billion in 1977 to a peak of \$2.44 billion in 1980, before falling to \$2.21 billion in 1981. Net earnings reflected the cyclical pattern of worldwide economic activity, rising from \$38.4 million in 1977 to a peak level of \$154.9 million in 1979, and falling off to \$3.3 million in 1981.

The severe drop in earnings in 1981 is attributable to three main factors, namely:

- significantly reduced prices and sales volumes for building materials products.
- a strike which closed the Company's major British Columbia operations for six to ten weeks.
- higher interest costs.

A review of the significant factors affecting sales and net earnings in each of the last five years follows.

1977:

The year 1977 saw continuing recovery in lumber markets from the cyclical low in 1975. Newsprint demand was firm, but margins for pulp, containerboard

and packaging products were squeezed by weak markets and rising costs. The Company wrote off its \$22.3 million interest in La Cellulose d'Aquitaine, a French pulp producer. Losses from the Company's transportation operations also depressed earnings in 1977.

During the year the Canadian dollar fell in value from U.S. \$.99 to U.S. \$.91. Because a sizeable portion of MacMillan Bloedel's sales and working capital are denominated in foreign currencies, this decline improved net earnings by approximately \$23 million.

1978:

During 1978 markets improved although price increases for containerboard and packaging were not sufficient to offset higher production costs.

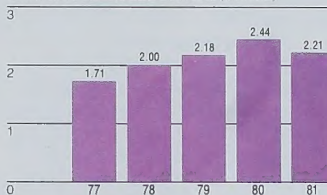
Equity earnings totalled \$9.4 million, an increase of \$6.2 million over the previous year. Approximately \$8.6 million of equity earnings in 1978 were due to foreign exchange gains from translating the working capital of Koninklijke Nederlandse Papierfabriek N.V. (KNP) into Canadian dollars. In 1978 the Company owned 44 per cent of the Common shares of KNP (subsequently increased to 48 per cent) which is a major producer of coated and uncoated paper for the European Economic Community.

During the year, the continued weakening of the Canadian dollar augmented net earnings by an estimated \$25 million, including the translation gain included in equity earnings.

1979:

Net earnings in 1979 amounted to \$154.9 million, despite work stoppages which cost an estimated \$29 million. Prices for pulp, lumber, newsprint, containerboard and packaging products were significantly higher, while prices for plywood improved modestly.

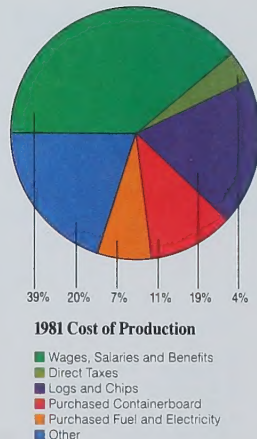
Sales of Products and Services (\$ billions)



Equity earnings fell to \$1.8 million, partly because of a provision for an expected loss with respect to a subsidiary of KNP and partly because of smaller exchange gains on the translation of KNP's financial statements into Canadian dollars.

A net profit of \$12.5 million was realized from the disposal of certain investments and subsidiaries.

Net earnings in 1979 benefited from a lower average income tax rate (39.1 per cent in 1979 as compared to 45.3 per cent in 1978) due to several factors, including an increase in investment tax credits and a low rate of tax on certain capital gains.



1981 Cost of Production

- Wages, Salaries and Benefits
- Direct Taxes
- Logs and Chips
- Purchased Containerboard
- Purchased Fuel and Electricity
- Other

1980:

In 1980 the Company's net earnings dropped 27 per cent to \$113.2 million. This reduction was largely attributable to the weakening of building materials markets, particularly during the second half of the year. Lower building materials prices caused the Raw Materials and Building Materials segment to incur losses during the final quarter of 1980.

Demand for newsprint, groundwood specialty papers, fine papers and kraft pulp remained strong and the Company's facilities operated at close to full capacity. Higher wood chip prices and other cost increases were only partially offset by price increases; hence profit margins declined in the Pulp and Paper segment.

Better market conditions and the acquisition of a corrugating medium facility and six container plants in Eastern Canada resulted in a \$13.6 million improvement in the operating profit of the Containerboard and Packaging segment. By the final quarter of the year, some market softness was evident in Eastern Canada and the United Kingdom, but markets remained firm in Western Canada and the United States.

During the fourth quarter of 1980, KNP recorded a small operating loss and made provision in its accounts for the cost of closing several old and uneconomic paper machines and a boxboard plant. These fourth quarter losses fully offset the \$6.8 million of equity earnings during the first nine months of 1980.

The average effective income tax rate in 1980 fell by 4.2 per cent due to several factors, including increased tax credits for investments and inventories, the release of tax provisions relating to prior years, and an increase in non-taxable foreign exchange translation gains.

1981:

During 1981 the Company's net earnings fell to \$3.3 million, which resulted in a loss of \$.53 per Common share after providing for preferred share dividends. These results include an extraordinary gain of \$30.0 million, or \$1.41 per Common share, from the sale of the Company's 65 per cent interest in MacMillan Rothesay Limited.

Sales in 1981 fell by \$227 million or 9.3 per cent; increased unit sales values were more than offset by decreased sales volumes.

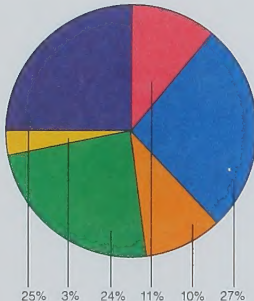
During 1981 lumber markets continued to deteriorate with further price erosion and a significant reduction in shipment volumes. As a result, the Raw Materials and Building Materials segment incurred an operating loss of \$82.2 million.

Newsprint markets remained firm but markets for pulp slowed in the latter part of the year. Production costs rose faster than prices, squeezing margins for both products during the year.

Containerboard and packaging markets in the United States and in Eastern Canada weakened considerably in the latter part of 1981. And while packaging markets in Western Canada

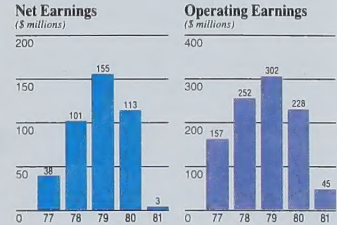
remained firm, markets in the United Kingdom remained depressed.

The Company's labour contracts with the principal unions at its British Columbia operations expired in mid-1981. Prolonged strikes ensued, reducing operating earnings by an estimated \$42 million. A two-year



1981 Sales by Product

■ Lumber
■ Panelboards
■ Newsprint and Fine Papers
■ Pulp
■ Containerboard and Packaging Products
■ Other



settlement was eventually reached which provided for wage increases of 15 per cent in the first year and 13 per cent in the second year, as well as for improved benefits and a cost of living clause.

During 1981 the Company recorded a loss on its equity investments of \$3.9 million which was, to a large extent, a result of the strengthening of the Canadian dollar relative to the currencies in which KNP conducts its business.

Income from investments totalled \$15.6 million, of which \$11.2 million was interest earned on funds held in escrow for various environmental protection and waste disposal capital expenditures in the United States. On the other hand, interest expense rose by \$31.3 million due to increased borrowing and higher rates of interest.

Selected Quarterly Financial Data

	1980				1981			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Sales and other income (\$ millions)	\$619.3	\$647.0	\$609.3	\$580.6	\$617.3	\$712.8	\$363.3	\$536.7
Net earnings (loss)								
Amount (\$ millions)								
– before extraordinary item	44.7	37.6	25.2	5.7	11.5	10.0	(38.4)	(9.8)
– after extraordinary item	44.7	37.6	25.2	5.7	11.5	10.0	(8.4)	(9.8)
Per Common share (dollars)								
(after preferred dividends)								
– before extraordinary item	2.04	1.71	1.12	.16	.40	.32	(2.00)	(.66)
– after extraordinary item	2.04	1.71	1.12	.16	.40	.32	(.59)	(.66)
Price range of Common shares on Toronto Stock Exchange (dollars)								
High	33.50	29.75	35.50	43.25	51.00	53.38	42.13	27.75
Low	25.50	24.25	29.25	30.50	35.50	38.75	26.00	20.00
Dividends per Common share (dollars)	.35	.35	.35	.70	.35	.35	.35	.10

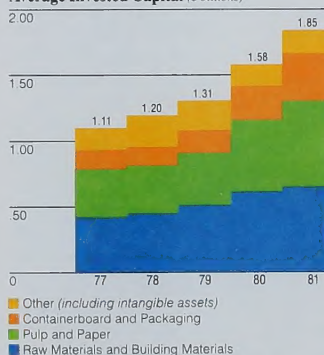
Return on Invested Capital

Return on invested capital is an important measure of the Company's performance. It is calculated as the ratio of net operating profit after taxes to average invested capital. Net operating profit after taxes is the sum of net earnings before extraordinary items and minority interests, the change in deferred income taxes, and interest expense net of associated current taxes. Invested capital is the average over a year of the sum of interest-bearing debt, deferred income taxes, minority interests, preferred share capital and common shareholders' equity. As

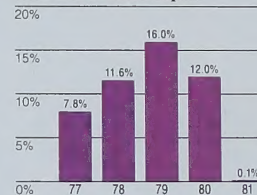
returns are determined before financing charges, this measure of operating profitability is independent of changes in the Company's financial structure or in interest rates and other costs of capital.

For each business segment, net operating profit after taxes as a percentage of capital invested in each segment also serves as a useful measure of performance. Charts on the following pages depict return on invested capital for each of the Company's three business segments.

Average Invested Capital (\$ billions)



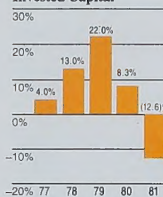
Return on Invested Capital



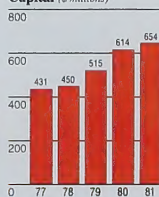
Raw Materials and Building Materials

Over the past five years, sales by the Raw Materials and Building Materials segment have accounted for approximately 47 per cent of total sales (before inter-segment eliminations). In 1981 sales from this segment totalled

Segment Return on Invested Capital



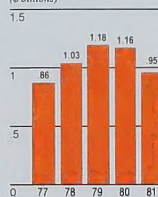
Segment Invested Capital (\$ millions)



Segment Operating Earnings(Loss) (\$ millions)



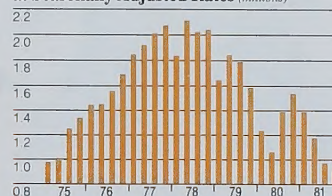
Segment Sales (\$ billions)



necessitated the closure of the Pine Hill particleboard mill in June 1980.

During 1981 high interest rates and limited mortgage funding persisted. Governments — particularly in North America — continued to fight inflation with restrictive monetary policies. As a result, by the third quarter of 1981 prices for most grades and species of

U.S. Housing Starts — by Quarter at Seasonally Adjusted Rates (millions)



\$947 million, of which \$108 million were transfers of logs and chips to other segments. Sales of products produced by others — either sold under agency agreements or purchased for resale through the Company's distribution centres — accounted for about 23 per cent of the remaining \$839 million.

Returns from the Raw Materials and Building Materials segment have demonstrated severe cyclical volatility over the last five years. This volatility stems from fluctuations in the level of worldwide construction activity, particularly in residential construction in the United States. As the graphs on this page illustrate, the profitability of the Company's Raw Materials and Building Materials segment tends to lag behind U.S. housing starts by about one year.

By the fourth quarter of 1979, however, U.S. residential construction had slowed down and North American markets for lumber and plywood weakened in response. Profitability from sales to overseas markets such as Europe and Japan remained strong well into 1980, partly because of the negotiation of sales contracts well in advance of shipment.

During 1980 North American lumber markets continued to weaken due to the impact of high interest rates on housing starts in both Canada and the United States. Offshore markets also declined during the latter part of the year. These market conditions, combined with continued cost escalation and winter logging conditions, resulted in fourth quarter operating losses for this segment. Moreover, adverse operating conditions

lumber fell to levels which led to the curtailment of production, and by the fourth quarter only half of the Company's productive capacity was being utilized. Plywood and waferboard markets also deteriorated to the point where production curtailments were necessary to avoid the accumulation of inventory.

Because of weak markets and the high interest cost to finance log inventories, most of the Company's logging operations in British Columbia were closed for prolonged periods in 1981, particularly towards the end of the year. Many operations remained closed well into the first quarter of 1982.

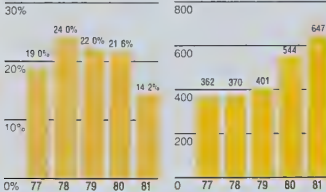


Clear cedar paneling adds natural beauty to homes and commercial buildings. MacMillan Bloedel manages 11 per cent of the world's standing inventory of old growth western red cedar.

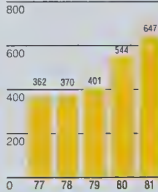
Pulp and Paper:

Over the past five years, the contribution of the Pulp and Paper segment to total sales (before inter-segment eliminations) has grown from 32 per cent in 1977 to 36 per cent in 1981. Pulp and Paper sales grew from \$576 million to \$831 million during this

Segment Return on Invested Capital

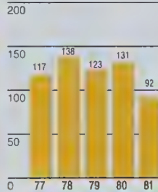


Segment Invested Capital (\$ millions)

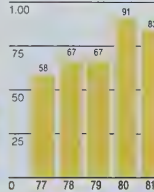


- market strength for newsprint and groundwood specialty papers during the entire period
- strong pulp markets from 1978 to mid-1981
- the decline of the Canadian dollar from approximately U.S. \$.99 in early 1977 to below U.S. \$.85 during 1981

Segment Operating Earnings (\$ millions)



Segment Sales (\$ billions)



period as a result of higher prices for all products, a higher value-added product mix, and expanded production capacity for newsprint and groundwood specialty papers. Annual effective capacity to produce newsprint and groundwood specialty papers increased from 1,157,000 tonnes at the beginning of 1977 to 1,360,000 tonnes by March 1981, when the Number 11 newsprint machine began operating in Powell River. On July 28, 1981 the Company sold its 65% interest in MacMillan Rothesay Limited, a New Brunswick newsprint producer with 310,000 tonnes of annual effective capacity.

Over the past five years, the Company's Pulp and Paper segment has provided relatively high and stable returns due to the following factors:

- significant capital spending to modernize the Company's newsprint mills
- an emphasis on high value-added, groundwood specialty grades.

In 1977 newsprint demand was strong, but the accumulation of large inventories of market pulp in Europe produced a collapse in pulp prices during the year.

Newsprint markets continued to be strong during 1978. Production curtailments by Scandinavian pulp producers, combined with improved demand, reduced most of the excess pulp inventory and led to a recovery in prices during the third quarter of 1978.

During 1979 markets for all pulp and paper products were strong, but a series of work stoppages in British Columbia and a seven month strike at the MacMillan Rothesay mill in New Brunswick resulted in lost production of approximately 53,000 tonnes of market pulp and 215,000 tonnes of newsprint



and groundwood specialty papers.

Markets for newsprint, groundwood specialties and pulp remained strong in 1980, but higher costs for wood, fuel, labour and chemicals squeezed profit margins.

During 1981 markets for newsprint and groundwood specialties remained firm, but price increases did not fully offset rising costs. Pulp markets softened during 1981, reflecting slow growth in most world economies. Strikes at the Company's principal pulp and paper facilities in British Columbia during 1981 resulted in lost production of approximately 78,000 tonnes of pulp and 182,000 tonnes of newsprint and groundwood specialty papers. This reduced segment operating profit by an estimated \$41 million.

The Far East and Western North America are major growth markets for MacMillan Bloedel's high-grade telephone directory paper.



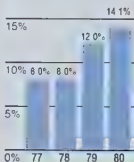
Pine Hill, Alabama's kraft pulp digester is 88 metres in height and annually provides 365,000 tonnes of furnish for the linerboard machine.

Containerboard and Packaging:

Sales of the Containerboard and Packaging segment have increased from \$308 million in 1977 to \$525 million in 1981. This growth in sales reflects higher product prices during the period

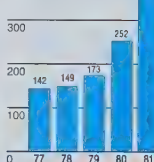
Segment Return on Invested Capital

20%



Segment Invested Capital (\$ millions)

400



and expanded productive capacity. In 1977 annual effective capacity stood at 453,000 tonnes of containerboard and 565,000 tonnes of corrugated containers. By year end 1981 these figures had increased to 535,000 tonnes of containerboard and 613,000 tonnes of corrugated containers, representing increases of 18.1 per cent and 8.5 per cent respectively. The most significant changes to operating capacity over the last five years were:

- the acquisition of the 71,000 tonne per year corrugating medium mill at Sturgeon Falls, Ontario in late 1979
- the acquisition of corrugated container plants in five Eastern Canada cities in late 1979 and early 1980, which increased annual effective capacity by 133,000 tonnes
- the sale of three non-profitable corrugated container plants in the

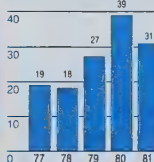
United States in late 1979 and early 1980, which reduced annual effective capacity by 67,000 tonnes

- the expansion of the Alabama mill's annual linerboard capacity by 14,000 tonnes.

In January, 1982 the Company completed an extension to the dryer

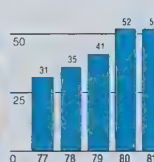
Segment Operating Earnings (\$ millions)

50



Segment Sales (\$ billions)

75



section of the linerboard machine at Pine Hill, Alabama which increased annual effective capacity by a further 50,000 tonnes. Construction of a 190,000 tonne per year corrugating medium line at Pine Hill is ahead of schedule and is expected to be completed in late 1982.

During 1977 and 1978 the Company's Containerboard and Packaging segment recorded an operating profit of \$19 million and \$18 million respectively. Product markets were generally unsettled, and price increases approximately offset rising costs.

During 1979 prices for containerboard and packaging products strengthened and operating profit improved. Extensive efforts to improve

the operating efficiency of the Company's container plants in the United States produced better results in the latter half of the year.

Generally better market conditions, combined with the acquisition of the corrugating medium mill and the six corrugated container plants in Eastern Canada, led to a significant improvement in operating earnings in 1980. However, by the last quarter of the year, packaging markets in the United Kingdom and Eastern Canada softened, although Western Canadian packaging markets and U.S. linerboard markets remained relatively healthy.

On September 26, 1980, the pulp digester at the Pine Hill linerboard complex had a major pressure failure, resulting in the closure of the mill until February 1981. Lost production totalled 88,000 tonnes in 1980 and 41,000 tonnes in 1981. The mill was insured for the damage incurred as well as for lost operating profit.

During 1981 packaging markets continued to be sluggish in the United Kingdom and Eastern Canada. Western Canadian packaging markets remained firm. During the first half of the year U.S. containerboard and packaging markets improved, but by the fourth quarter demand weakened materially, due to the poor performance of the U.S. economy. This led to lower product prices and to some curtailment of linerboard production at Pine Hill. In addition, due to adverse market conditions, the Company has not operated its linerboard machine at Port Alberni, B.C. since October 1981.

Foreign Exchange

The Company's Canadian operations presently generate an annual net inflow of approximately 500 million U.S. dollars.

The weakness of the Canadian dollar in recent years has had a positive impact upon MacMillan Bloedel's revenues, earnings and cash flow. Apart from the effect of translating various balance sheet items, a one per cent change in the Canadian dollar exchange rate relative to the U.S. dollar changes after tax earnings by approximately \$3.2 million or 15 cents per Common share.

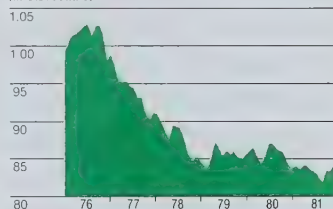
The Company follows a policy of entering into foreign exchange contracts whereby it agrees to deliver its expected net U.S. dollar receipts for a set amount of Canadian dollars at dates up to 12 months in the future. These contracts eliminate the risk of loss due to the Canadian dollar strengthening between the date of entering into the contract and actual conversion, but conversely result in the Company foregoing any gain that might arise from a weakening of the Canadian dollar.

In 1981 the Company's sales denominated in U.S. dollars were translated into Canadian dollars at an average rate of U.S. \$.834 dollars per

Canadian dollar as compared to an average rate of U.S. \$.855 in 1980.

The value of the Canadian dollar during 1981 fluctuated between U.S. \$.805 and U.S. \$.850. As of December 31, 1981 the Company had sold forward U.S. \$334 million at an average rate of U.S. \$.818 per Canadian dollar.

The Canadian Dollar
(in U.S. dollars)



Impact of Inflation

The Company's audited financial statements are prepared in accordance with accounting principles generally accepted in Canada. These statements reflect historical costs and accordingly do not highlight the problems arising from inflation. Various regulatory bodies have attempted to develop an effective means to illustrate the impact of inflation, but so far no consensus as to which is the most appropriate method has been reached. MacMillan Bloedel's presentation on page 37 of this report does not attempt to adjust its financial statements for all aspects of inflation, but does present a simple illustration of the key problems arising from continued high levels of inflation.

Financial Charges

Between 1977 and 1979 the Company's total interest charges remained virtually constant at approximately \$33 million per year.

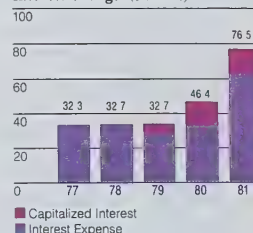
In 1980 total interest charges increased to \$46.4 million due to higher interest rates and to increased levels of interest-bearing debt. During that year, \$181.5 million of new fixed rate debt was raised at rates ranging from 8.25% to 12.5%. In addition, the amount of floating rate debt outstanding increased by \$106.5 million to \$131.7 million by the end of 1980. The interest rate on this floating rate debt averaged approximately 12.8% during 1980.

In 1981 interest charges increased to \$76.5 million and total interest-bearing debt increased by \$125.2 million. Almost two-thirds of the new debt raised carried floating rates of interest which averaged about 15.1% for the year.

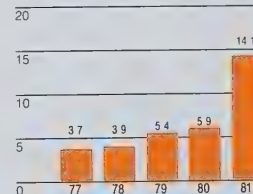
Interest charges related to major capital projects during construction are added to the cost of the assets rather than being included as interest expense on the statement of earnings. This capitalized interest is amortized over the economic life of the assets.

In addition to raising debt, the Company issued \$128 million of preferred shares in late 1980 and 1981. Thus preferred dividends increased by \$8.3 million during 1981.

Interest Charges (\$ millions)



Preferred Dividends (\$ millions)



Five Year Financial Data

(\$ millions except percentages)

	1977	1978	1979	1980	1981
Cash flow from operations	\$ 137.1	\$ 200.6	\$ 257.6	\$ 245.9	\$ 32.8
Depreciation, depletion, and amortization	80.0	75.6	82.6	88.7	92.0
Capital expenditures	77.4	121.6	280.4	327.7	307.9

Current assets	\$ 592.0	\$ 652.9	\$ 690.1	\$ 774.8	\$ 721.7
Current liabilities	299.0	351.9	370.1	353.1	408.5
Working capital	293.0	301.0	320.0	421.7	313.2
Non-cash working capital	253.0	294.0	328.8	477.5	434.4
Total assets	1,360.9	1,549.3	1,691.9	2,075.2	2,172.1

Short term interest-bearing debt	\$ 78.3	\$ 70.1	\$ 39.0	\$ 79.9	\$ 126.3
Long term debt	309.8	341.7	323.1	550.8	596.8

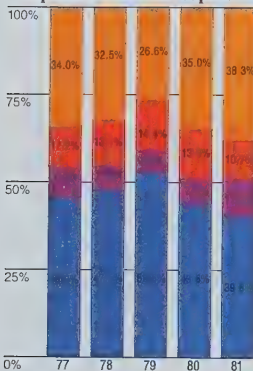
Total interest-bearing debt	388.1	411.8	362.1	630.7	723.1
Redeemable term preferred shares	88.0	88.0	88.0	88.0	116.0
Redeemable convertible preferred shares	—	—	—	50.0	95.9
Common equity, including retained earnings	524.9	601.8	714.3	783.4	752.7
Minority interests	22.6	20.6	21.6	23.0	6.1

Total invested capital before deferred income taxes	1,023.6	1,122.2	1,186.0	1,575.1	1,693.8
Deferred income taxes	116.5	145.1	174.8	226.9	196.1
Total invested capital	\$1,140.1	\$1,267.3	\$1,360.8	\$1,802.0	\$1,889.9

Debt as a percentage of invested capital

— before deferred income taxes	37.9%	36.7%	30.5%	40.0%	42.8%
— including deferred income taxes	34.0%	32.5%	26.6%	35.0%	38.3%

Composition of Invested Capital*



*At year end

- Debt
- Deferred income taxes and minority interests
- Preferred shares (with over five years remaining to maturity)
- Common shareholders' equity

Financial Position

Financial Flexibility

An important requirement for ensuring a firm's long term financial flexibility is the maintenance of a well balanced financial structure. The Company is working to improve its competitive position and to expand its productive capacity in those areas of the forest products business with the greatest potential for higher and more stable returns for shareholders. However, forest products markets will always retain a significant degree of sensitivity to cyclical changes in economic activity. The Company therefore maintains a prudent financial structure so as to preserve its financial integrity when faced with adverse operating conditions such as poor markets or prolonged strikes. Financial conservatism must, however, be balanced against the advantage of the relatively low after tax cost of debt capital. The graph on the page opposite depicts MacMillan Bloedel's financial structure over the past five years.

An effective method of enhancing a firm's long term financial flexibility is to establish the capability to raise funds from many sources. In order to gain access to funds where they are most readily available and on the most advantageous terms, the Company

maintains a presence in most of the world's major financial markets. MacMillan Bloedel's Common shares are listed on the New York Stock Exchange as well as on the principal Canadian exchanges. Over the past five years the Company has raised approximately \$340 million in Canada, \$175 million in the United States, and \$190 million in Europe.

Long term contractual lines of credit, with terms of 10 to 15 years, provide another means of enhancing long term liquidity. As of December 31, 1981, MacMillan Bloedel had long term lines aggregating \$593 million of which \$489 million remained unutilized.

The Company has available a number of sources of short term funds including \$117 million of short term bank lines of credit, up to \$60 million of commercial paper in the Canadian market and up to U.S. \$150 million of Bankers' Acceptances in the United States market.

Sources of Funds

Over the past five years internally generated cash flow has met approximately 50 per cent of the Company's fund requirements. The residual funds required were derived from the sale of assets or by raising new long term capital.

From 1977 to 1979 the Company raised most of its new long term capital by issuing U.S. \$85 million of term preferred shares in 1977 and U.S. \$100 million of long term debt in Europe during 1977 and 1978.

During 1980 \$245.9 million of operating cash flow was supplemented

with \$296.2 million of new long term financings. The major financings were U.S. \$65 million of tax-exempt industrial revenue bonds, a U.S. \$50 million ten year bank loan, a 12 year loan of 60 million Dutch guilders (approximately \$34 million), and \$50 million of Class B Convertible Preferred shares.

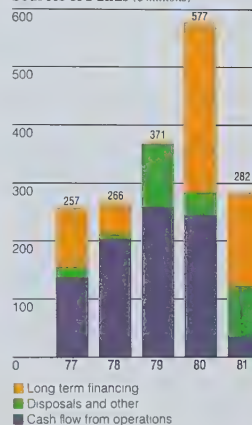
During 1981 the Company raised \$160 million of new long term capital. In February, the Company issued a second \$50 million series of Class B Convertible Preferred shares, carrying a dividend rate of 8.32%. In June, a third series of Class B Preferred shares was issued for an aggregate amount of \$28 million. This series carries a dividend of 1 $\frac{3}{4}$ % plus one-half of the Bank Prime Rate and has a minimum term of ten years. It has no conversion feature.

The \$128 million of preferred shares issued in 1980 and 1981 strengthened the Company's balance sheet and, together with operating cash flow, formed the base for the Company's capital program.

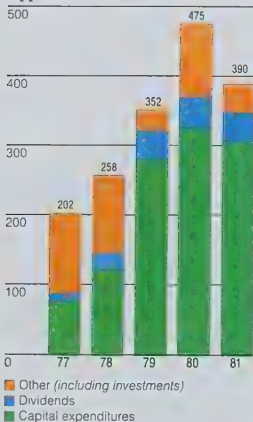
During 1981 \$82 million of new long term debt was raised, including a ten year term loan of 40 million Dutch guilders (approximately \$19 million) carrying a rate of 12 $\frac{7}{8}$ %. The majority of the residual increase in long term debt was derived by drawing down on the Company's contractual long term lines of credit.

Over the last five years funds have also been derived from the sale of assets that did not meet the Company's

Sources of Funds (\$ millions)



Application of Funds (\$ millions)



investment criteria. The divestiture of four packaging plants generated proceeds of \$5 million in 1979 and \$17 million in 1980. In 1981 the Company realized \$103 million from the sale of its interest in the MacMillan Rothsay newspaper mill in St. John, New Brunswick.

Application of Funds

Funds generated from operations, complemented by funds raised by issuing long term securities or by disposing of assets, are available for capital expenditures, for dividends and for "other" applications, including investments, the repayment of long term debt, and the reduction of minority interests. Over the past five years capital expenditures have accounted for \$1.115 billion or 66 per cent of total applications, dividends for \$168 million or 10 per cent, and "other" applications for \$395 million or 24 per cent.

Any amounts not so applied result in an increase in working capital; any shortfall results in a reduction in working capital.

"Other" Applications

Over the past five years, \$179 million of long term debt has been repaid. The repayment schedule graph on the opposite page illustrates future commitments as of December 31, 1981, to retire long term debt and term preferred shares. The average maturity of the Company's long term debt and term preferred shares is approximately 8 years.

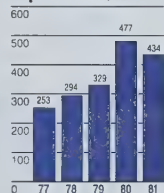
"Other" applications also include \$187 million of investments, the most significant of which was \$73.2 million in 1978 for an 18.9 per cent interest in Domtar Inc. (This investment was subsequently disposed of in 1979.) The principal component of "other" applications in 1980 was \$76.0 million for funds held in escrow from the proceeds of tax-exempt bonds issued primarily to finance environmental protection and waste disposal expenditures which are part of the Pine Hill expansion project.

The Company's working capital is comprised of its net cash position (cash and marketable securities less short term indebtedness) plus non-cash working capital. This latter category equals the sum of accounts receivable, inventories, prepaid expenses and current items of deferred income taxes, less accounts payable and various accrued liabilities.

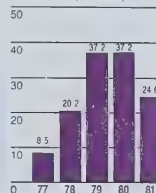
The net cash portion of working capital is available in future years for investment, for the reduction of liabilities or for distribution as dividends. However, increases in non-cash working capital are required for the continuing operation of the Company and accordingly are not available for distribution to shareholders. Over the past five years these increases have averaged \$31 million per year. This represents an average annual increase of 9 per cent and is primarily attributable to inflation. However, some of the growth in non-cash working capital stems from increased sales volumes resulting from the expansion of operating capacity over the period.

In 1980 non-cash working capital increased by \$148 million, primarily due to the accumulation of logs and lumber near the end of the year because of very weak building materials markets. During 1981 the Company initiated a program to reduce these inventories. Consequently, non-cash

Non-Cash Working Capital (\$ millions)



Common Share Dividends (\$ millions)



working capital was reduced by \$43 million from the previous year end.

Dividends

Dividend payments to preferred shareholders increased substantially in 1981 due to the issue of \$100 million of convertible preferred shares in late 1980 and early 1981 and the issue of \$28 million of term preferred shares in June 1981.

Dividends paid to Common shareholders increased from \$8.5 million in 1977 (\$.40 per share) to \$37.2 million in both 1979 and 1980 (\$1.75 per share). For the first three quarters of 1981 the Company's regular quarterly dividend was 35 cents per share, but it was reduced in the fourth quarter to 10 cents per share. This

Capital Expenditures 1977 to 1981 (\$ millions)

Business Segment	1977	1978	1979	1980	1981	Five Year Total	% of Total
Raw Materials and Building Materials							
Raw Materials	\$ 32.0	\$ 53.0	\$ 56.5	\$ 41.6	\$ 48.2	\$ 231.3	20.7%
Building Materials	9.7	15.9	62.9	46.8	10.0	145.3	13.0%
Pulp and Paper	24.2	37.3	118.3	183.0	105.3	468.1	42.0%
Containerboard and Packaging	9.4	13.7	36.8	47.5	133.2	240.6	21.6%
Other	2.1	1.7	5.9	8.8	11.2	29.7	2.7%
Total	\$ 77.4	\$ 121.6	\$ 280.4	\$ 327.7	\$ 307.9	\$ 1,115.0	100.0%

reduced 1981 dividends to \$24.6 million or \$1.15 per Common share.

The Company's normal policy is to maintain a regular quarterly dividend reflecting the firm's fundamental earning power and the long term economic outlook. During 1981 markets for building materials products deteriorated to the extent that the Company incurred a loss on operations. With no material improvement in sight, and with the high cost of incremental borrowing, financial prudence dictated the temporary reduction of Common share dividends to a level of 10 cents per quarter, starting in the fourth quarter of 1981.

Capital Expenditures

One of MacMillan Bloedel's primary objectives is to increase the value of its shareholders' investment by improving the rate of return on the capital invested in its various lines of business. In order to improve the return on invested capital, the Company has implemented strategies aimed at increasing the return on the existing asset base, expanding in those areas which will provide the

highest returns, and disposing of facilities or other assets which do not provide satisfactory returns or do not complement corporate strategy. Capital funds are allocated to new discretionary investments on the basis of their expected discounted cash flow return on investment.

Over the past five years the Company's capital expenditures have totalled \$1.115 billion and are tabulated above by business segment.

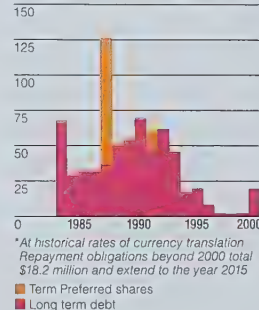
During 1981 capital expenditures totalled \$308 million, of which approximately 40 per cent were for projects necessary to keep the Company's operations in good working order and environmentally sound. The remaining 60 per cent were for discretionary expenditures to improve cost effectiveness and expand capacity, thereby improving the Company's fundamental earning power. During 1981 approximately \$110 million was directed towards the Pine Hill, Alabama expansion project, the first phase of which has recently reached completion.

Because of the impact of the

current adverse operating environment, virtually no new discretionary projects will be undertaken until conditions improve. Moreover, the completion of the \$92 million recovery boiler at the Harmac pulp mill and the \$49 million fine paper machine at Island Paper Mills — both already under construction — have also been deferred. However, the Company is proceeding with the Pine Hill expansion project since the bulk of the spending has already been committed and a substantial amount of the required capital has been prefunded by the issuance of tax-exempt industrial revenue bonds. The capital program in 1982 is planned at approximately \$240 million, of which \$140 million relates to the Pine Hill expansion project. A portion of the remaining expenditures are required to keep the Company's operations in good working order and environmentally sound. Currently, a program of capital spending restraint is aimed at reducing expenditures in 1982 from the planned level of \$240 million.

The most significant of the Company's recent capital projects are reviewed on the next few pages.

Repayment Schedule at December 31, 1981 for Long Term Debt and Term Preferred Shares* (\$ millions)



*At historical rates of currency translation. Repayment obligations beyond 2000 total \$18.2 million and extend to the year 2015

Capital Program

Raw Materials and Building Materials

During 1981 capital expenditures in Raw Materials aggregated \$48 million, including \$23 million for timber and timberland, \$4 million for main logging roads in British Columbia, and \$21 million for logging equipment.

In addition to these capital expenditures, the Company spent approximately \$14 million for its forestry program in British Columbia. In 1981 the Company planted 27 million seedlings, principally in British Columbia and Alabama, bringing the total seedlings planted to 263 million.

Capital expenditures for Building Materials facilities aggregated \$10 million during the year.

Alberni Pacific Division

MacMillan Bloedel's new Alberni Pacific Division sawmill has an annual effective capacity of 216 million board feet per year and was constructed at a cost of \$54 million.

Since startup on September 8, 1980 the mill's productivity and efficiency has improved steadily, surpassing pro forma operating specifications by the end of 1981.

Workers were fully involved from the mill's conception, and there has been a steady input of useful suggestions from the mill's employees. Their involvement and performance have been instrumental to the success of the new facility.

How the Mill Functions

The process starts when either of two log side lifts (1) raise bundles of logs from the log pond up to the log deck. Two 15-tonne grapple cranes (2) then break open the steel strapping from the bundles and lift individual logs onto conveyers that lead to debarkers. These debarkers (3) have steel arms that revolve around the logs stripping away the bark which is carried off and ground into hog fuel for burning in the power house to produce steam.

From here logs are squared off at one of two cut-off saws (4) with the assistance of computer controls to measure the size of each log. This data helps the cut-off saw operator to direct the larger logs to the nine-foot bandsaw headrig (6) and medium-sized logs (up to 30 inches) to the log quad headrig (5).

At the log quad headrig a computer scans each log for size and shape, and adjusts the position of the quad saw's chipper heads and its four bandsaws. The chips are used as furnish for the nearby Alberni pulp and paper mill. Pieces of lumber from the outside of the log are conveyed to an edger, while the larger pieces (cants) are directed to the cant quad saw (8).

The larger logs (up to 60 inches) are directed to the nine-foot headrig (6), where they are cut into slabs or cants. The outside pieces are transferred to the horizontal twin resaw (7), the larger square-edged pieces to the cant quad saw (8), and the other pieces to an edger. The extreme outside pieces are sent to a chipper.

The horizontal twin resaw (7) cuts slabs up to 3 feet wide to the desired final thickness. Most of the resulting pieces are directed to an edger, although some are recirculated for another pass.

The cant quad saw (8) consists of four six-foot vertical bandsaws, which reduce cants to double or triple their final thickness, and in some cases to final thickness. After the cut, the cant quad operator can route the wood to a vertical twin bandsaw (9), to an edger (10), or to the trimmers (11).

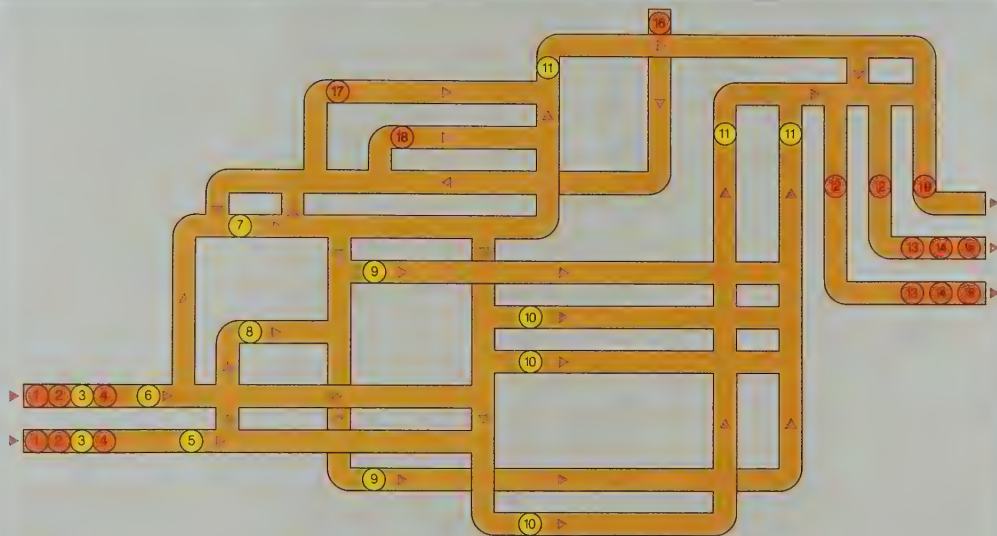
The vertical twin band mills (9) cut wood down to a size meeting customers' specifications, after which the lumber is sent to the trimmers (11).

The lumber is cut to length in the trimmers; from here the wood proceeds to the automatic bin sorters (12), and finally for bundling (13 and 14) and dipping in a preservative bath (15).

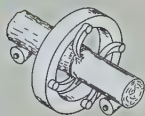
Wood from the trim lines which does not have the required thickness to make it a saleable product re-enters the mill and is directed to the "reman" system which consists of a single vertical resaw (17) and a three-saw edger (18).



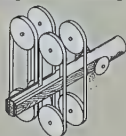
The Company built nearly 400 kilometres of logging roads in 1981 through the rugged terrain on the British Columbia coast.



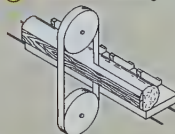
③ Debarkers



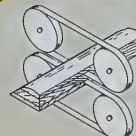
⑤ Log Quad Headrig



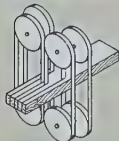
⑥ Bandsaw Headrig



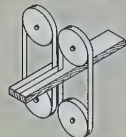
⑦ Horizontal Twin Resaw



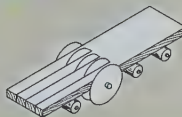
⑧ Cant Quad Saw



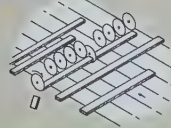
⑨ Vertical Twin Bandsaws



⑩ Edgers



⑪ Trimmers



Hemlock and Balsam lumber en route to customers around the world awaits loading.

Alberni Pacific Division Sawmill

- Side Lifts
- Grapple Cranes
- Cut-off Saws
- Automatic Sorters
- Stackers
- Strappers
- Preservative Baths
- Re-entry to Remanufacturing Area
- Reman Single Vertical Bandsaw
- Reman Edger
- Green Chain



Scheduled for startup in late 1982, construction of Pine Hill's new corrugating medium machine is moving ahead. The 'bed' for the new machine is shown above and a general view of the expansion activity is shown on the right.



Containerboard and Packaging

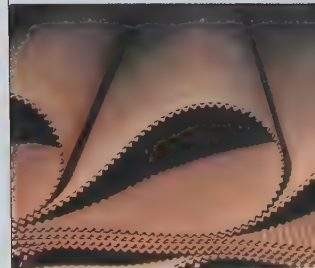
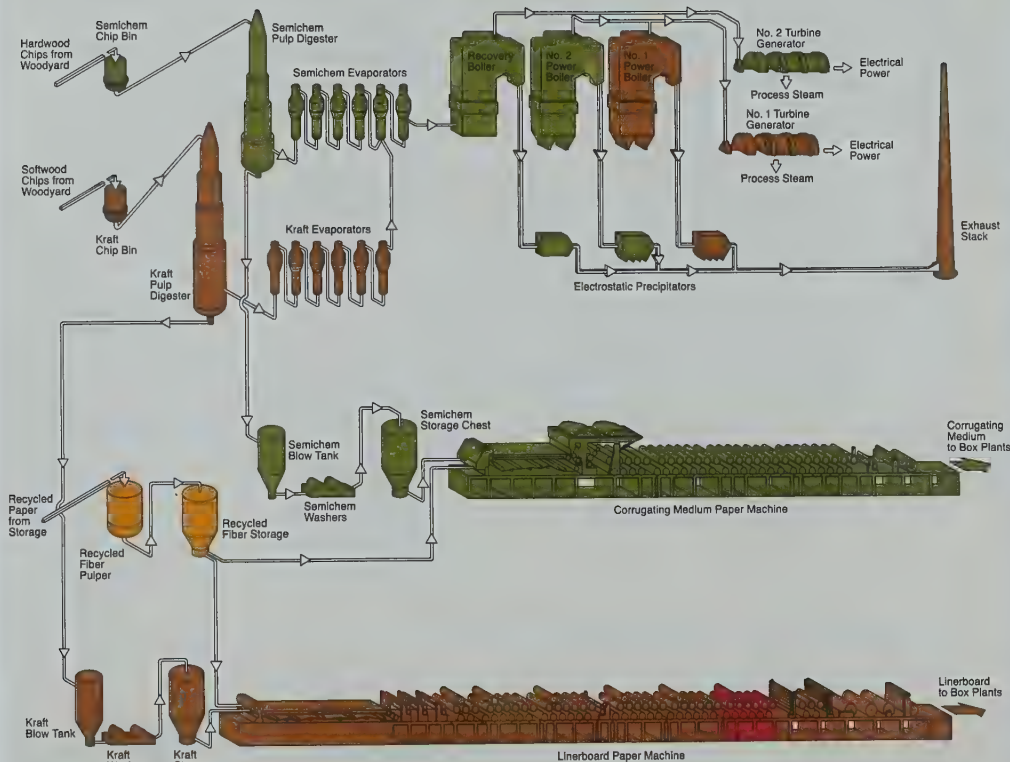
During 1981 capital expenditures in the containerboard and packaging segment totalled \$133 million. Of this amount \$110 million was accounted for by the Pine Hill expansion project. The first phase of this project was completed in January 1982. It increased the annual capacity of the existing linerboard machine by 50,000 tonnes by adding additional drying capacity which, in turn, facilitated faster running speeds. This first phase also included a new

recycled fibre pulping unit which will provide furnish for both the linerboard machine and a new corrugating medium machine which is now under construction.

The new corrugating medium facility will have an annual effective capacity of 190,000 tonnes and is scheduled to begin production in late 1982. It will utilize a combination of hardwood fibre and recycled paper. Since the forests surrounding Pine Hill contain substantial inventories of under-utilized hardwoods, the new

medium mill will provide a better balance between our conversion facilities and the available timber resource.

The Pine Hill project also includes a new recovery boiler for the existing linerboard machine and the conversion of the existing recovery boiler to a power boiler capable of burning wood residuals and coal, as well as oil or natural gas. The project will improve environmental control and reduce the mill's fuel oil consumption by an estimated 350,000 barrels per year. This represents an annual saving of \$12 million, given present fuel oil prices.



The first stage in producing corrugated containers is to 'flute' corrugating medium to give its wave-like appearance and to glue it to linerboard to make 'single face' which is illustrated above.

Pine Hill Expansion

- Additional drying capacity (linerboard machine)
- New recycled fibre pulping facilities
- New semi-chemical pulping facilities and corrugating medium machine
- Facilities prior to expansion



Powell River's new \$21 million hog fuel dryer and precipitator will do much to reduce energy costs and meet B.C.'s stringent air emission standards. Powell River's No. 11 paper machine, above right, started up in March, 1981.



Pulp and Paper

During 1981 capital expenditures in the pulp and paper segment totalled \$105 million. Of this amount, \$19 million was spent to complete the Number 11 paper machine in Powell River, B.C. This machine, together with related facilities, was constructed at a cost of \$171 million and started commercial production in March, 1981. The machine had a successful startup and is currently operating at a rate close to its effective capacity of 160,000 tonnes per

year. Related facilities for the project include:

- a double refiner line to produce thermomechanical pulp
- roll wrapping and finishing facilities
- additions to storage and ocean shipping facilities
- hog fuel and chip unloading facilities and conveyors
- expanded electrical power facilities.

Also at Powell River the Company completed construction of a \$21 million hog fuel dryer and precipitator. Hot flue gases from three power boilers are directed through a two-chamber, two-field electrostatic precipitator which

removes salt and fly ash to assure that current air emission standards are met. The cleaned flue gases, still containing valuable heat, then pass through large revolving cylinders containing wet hog fuel (bark and sawdust). The contact with the hot gases dries the hog fuel, thereby facilitating more efficient combustion in the mill's power boilers. This process will reduce fuel oil consumption by an estimated 195,000 barrels per year, which represents an annual cost saving, at current fuel prices, of approximately \$5 million.

	Year ended December 31		
	1981	1980	1979
	(\$000)		
Sales and other income:			
Sales of products and services	\$2,209,670	\$2,436,415	\$2,180,318
Income from investments	15,596	5,118	10,329
Profit on disposition of non-current assets	4,870	14,683	13,963
	2,230,136	2,456,216	2,204,610
Costs and expenses (Note 13(a)):			
Cost of sales and services	2,013,073	2,062,765	1,770,656
Selling, general and administrative	203,849	181,383	147,994
Interest	63,177	31,857	28,878
	2,280,099	2,276,005	1,947,528
Earnings (loss) before income taxes and other undernoted items	(49,963)	180,211	257,082
Income taxes (Note 13(b)):			
Current	7,620	7,215	63,905
Deferred	(38,946)	55,753	36,466
	(31,326)	62,968	100,371
Earnings (loss) before undernoted items	(18,637)	117,243	156,711
Equity in earnings (losses) of partly-owned companies (Note 4)	(3,865)	(17)	1,815
Minority interests in subsidiaries	(4,188)	(4,041)	(3,624)
Earnings (loss) before extraordinary item	(26,690)	113,185	154,902
Extraordinary item (Note 13(c))	29,997	—	—
Net earnings	\$ 3,307	\$ 113,185	\$ 154,902
Net earnings (loss) per Common share (after providing for preferred share dividends) (dollars) (Note 13(d)):			
Before extraordinary item	\$(1.94)	\$5.03	\$7.03
After extraordinary item	\$(.53)	\$5.03	\$7.03

MacMillan Bloedel Limited
Consolidated Statements

Earnings

MacMillan Bloedel Limited
Consolidated Statements

Balance Sheets

Assets	December 31	
	1981	1980
	(\$000)	
Current assets:		
Cash	\$ 4,277	\$ 1,064
Short term investments and deposits, at cost which approximates market value	17,455	26,757
Accounts receivable less allowance for doubtful accounts		
Trade	234,928	265,105
Other	23,942	39,632
Inventories (Note 3)	416,941	422,940
Prepaid expenses	7,201	5,838
Deferred income taxes, current items	16,946	13,462
	721,690	774,798
Investments and other assets:		
Partly-owned companies, accounted for by the equity method (Note 4)	66,580	68,853
Other investments and assets, at cost	18,260	8,203
	84,840	77,056
Funds held for construction projects (Note 7(b))	74,351	76,046
Property, plant and equipment:		
Buildings and equipment, at cost (Note 5)	1,719,088	1,549,669
Less: Accumulated depreciation (Note 2)	785,492	764,164
	933,596	785,505
Construction in progress, at cost (Note 5)	185,460	193,031
	1,119,056	978,536
Timber, at cost less accumulated depletion	116,948	110,615
Logging roads, at cost less amortization	17,783	19,570
Land, at cost	12,519	12,291
	1,266,306	1,121,012
Intangible assets, at cost less amortization:		
Unallocated purchase price of shares in subsidiaries	19,201	20,401
Financing expenses	5,750	5,917
	24,951	26,318

The consolidated financial statements have
been approved by the Board of Directors:

C. C. Knudsen, Director

R. V. Smith, Director

\$2,172,138 **\$2,075,230**

Liabilities	December 31	
	1981	1980
	(\$000)	
Current liabilities:		
Short term bank indebtedness (Note 6)	\$ 129,545	\$ 73,392
Notes payable	13,400	10,263
Trade accounts payable	106,295	126,568
Accrued payroll and related liabilities	91,768	84,865
Accrued interest on borrowed funds	17,130	16,253
Other accounts payable and accrued liabilities	26,366	19,533
Income taxes payable	5,204	6,763
Current portion of long term debt (Note 9)	18,801	15,508
	408,509	353,145
Long term debt:		
Bonds and debentures (Note 7(a))	353,381	367,303
Term bank loans (Note 8)	223,727	160,151
Other liabilities (secured)	19,682	23,349
	596,790	550,803
Deferred income taxes	196,134	226,859
Minority interests in subsidiaries	6,259	23,117
	1,207,692	1,153,924
Shareholders' Equity		
Share capital:		
Shares without par value (Note 10)		
Authorized –		
3,400,000 Class A Preferred		
8,000,000 Class B Preferred		
35,000,000 Common		
Outstanding –		
Preferred –		
3,400,000 Class A	87,954	87,954
1,848,470 Class B, Series 1	46,212	50,000
1,986,700 Class B, Series 2	49,668	—
280,000 Class B, Series 3	28,000	—
Common –		
21,419,193 Common	177,144	171,415
	388,978	309,369
Retained earnings	575,468	611,937
	964,446	921,306
Commitments (Notes 10 and 11)		
Contingent liabilities (Note 12)		
	\$2,172,138	\$2,075,230

Changes in Financial Position

	Year ended December 31		
	1981	1980	1979
	(\$000)		
Source of working capital:			
Operations –			
Earnings (loss) before extraordinary item	\$ (26,690)	\$ 113,185	\$ 154,902
Depreciation, depletion and logging road amortization	91,965	88,732	82,586
Deferred income taxes, non-current portion	(37,465)	52,038	29,695
(Profit) loss on disposition of non-current assets	(4,870)	(14,683)	(13,963)
Other components not affecting working capital, net	9,896	6,571	4,409
	32,836	245,843	257,629
Class B Preferred shares –			
Net proceeds of issue	76,923	48,902	—
Conversions to Common shares (Series 1 and 2)	(4,120)	—	—
Common shares	5,729	—	240
Net proceeds of long term debt	81,529	247,303	4,348
Proceeds on disposition of non-current assets	12,220	34,903	108,542
Disposal of business (net of working capital of \$28,676,000) (Note 13(c))	74,818	—	—
Capital contributed by minority shareholder	2,004	—	—
	281,939	576,951	370,759
Application of working capital:			
Property, plant and equipment	307,856	327,692	280,443
Funds held for construction projects	(1,695)	76,046	—
Investments and other assets	13,026	4,754	3,071
Reduction in long term debt	30,428	21,079	23,043
Dividends – Shareholders of the Company	38,699	43,079	42,575
– Minority shareholders of subsidiaries	2,077	2,211	2,634
Other	20	405	—
	390,411	475,266	351,766
Increase (decrease) in working capital	(108,472)	101,685	18,993
Working capital at beginning of year	421,653	319,968	300,975
Working capital at end of year	\$313,181	\$421,653	\$319,968

	Year ended December 31		
	1981	1980	1979
		(\$000)	
Balance at beginning of year	\$611,937	\$542,929	\$430,602
Net earnings	3,307	113,185	154,902
	615,244	656,114	585,504
Deduct:			
Dividends:			
Preferred shares			
Class A	5,510	5,335	5,349
Class B, Series 1	3,783	516	—
Class B, Series 2	3,388	—	—
Class B, Series 3	1,454	—	—
Common shares – \$1.15 per share in 1981 and \$1.75 in 1980 and 1979	24,564	37,228	37,226
	38,699	43,079	42,575
Costs of issue of Class B Preferred shares, less applicable income taxes of \$950,000 in 1981 and \$962,000 in 1980	1,077	1,098	—
	39,776	44,177	42,575
Balance at end of year	\$575,468	\$611,937	\$542,929

MacMillan Bloedel Limited
Consolidated Statements

Retained Earnings

Auditors' Report

To the Shareholders of MacMillan Bloedel Limited:

We have examined the consolidated balance sheets of MacMillan Bloedel Limited as at December 31, 1981 and 1980 and the consolidated statements of earnings, retained earnings and changes in financial position for the years ended December 31, 1981, 1980 and 1979. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at December 31, 1981 and 1980 and the results of its operations and the changes in

its financial position for each of the three years in the period ended December 31, 1981 in accordance with generally accepted accounting principles consistently applied during the period except for the change, with which we concur, in the method of accounting for depreciation, as described in Note 2 to the financial statements.

PRICE WATERHOUSE
Chartered Accountants

February 19, 1982
Vancouver, B.C.

Notes to Consolidated Financial Statements

December 31, 1981, 1980 and 1979

In these financial statements "MacMillan Bloedel" means MacMillan Bloedel Limited and its consolidated subsidiaries, and "Company" means MacMillan Bloedel Limited as a corporation.

1. Accounting policies:

MacMillan Bloedel follows accounting principles generally accepted in Canada. Information with respect to differences between generally accepted accounting principles in Canada and the United States is provided in Note 16.

(a) Principles of consolidation –

The accompanying financial statements represent the consolidation of the financial statements of the Company and all its subsidiaries except Embrasca-Empreendimentos Florestais e Agricolas Ltda. (Embrasca) and its subsidiaries. The Company owns 51% of the voting shares of Embrasca but the terms of a shareholders' agreement make it inappropriate to consolidate the corporation and its subsidiaries. Instead, the investment in the corporation is accounted for by the equity method (Note 1(d)).

(b) Foreign currency translations –

A number of subsidiaries and partly-owned companies operate in foreign countries. In addition, substantial volumes of transactions of the Company and certain of its Canadian subsidiaries are denominated in foreign currencies. Transactions are covered by forward exchange contracts where considered appropriate, in which case, foreign exchange translations are made at such forward exchange contract rates. In all other cases, current assets (except inventories) and current liabilities are translated at the rates of exchange in effect as at the balance sheet dates, other assets (and related depreciation, depletion and amortization) and liabilities, at the rates in effect at the dates on which the assets were acquired or the liabilities were incurred, and items affecting net earnings (other than depreciation, depletion and amortization) at the average rates for the year. The net effect of the translation of foreign currencies is included in consolidated net earnings (Note 16(a)).

(c) Valuation of inventories –

Inventories of substantially all operating and maintenance supplies and logs, poles, pulp chips, pulpwood and cordwood are valued at the lower of average cost and replacement cost. Inventories of manufactured products are valued at the lower of average cost and net realizable value.

(d) Partly-owned companies –

Investments in partly-owned companies, including joint ventures, are accounted for by the equity method. Under this method, MacMillan Bloedel's share of the net earnings of the partly-owned companies is included in consolidated net earnings.

(e) Property, plant and equipment –

The costs of maintenance, repairs, minor renewals or replacements and spur logging roads are expensed as incurred. The costs of major replacements, extensions or improvements and main logging roads are capitalized in the property, plant and equipment accounts. On retirement or disposal of property, plant and equipment, the costs thereof and the related accumulated depreciation or depletion are eliminated from the financial statements and any profits or losses are reflected in the consolidated statements of earnings.

For years prior to 1980, depreciation was computed on a straight-line basis on original cost. In 1980 MacMillan Bloedel adopted the units-of-production basis for depreciation of manufacturing assets (Note 2). Non-manufacturing assets continue to be depreciated on a straight-line basis.

Depletion of timber and amortization of main logging roads are determined on a basis related to log production.

The rates of depreciation being applied are intended to fully depreciate manufacturing assets (at normal production levels) and non-manufacturing assets over the following periods:

Buildings	20 and 40 years
Pulp and paper mill machinery and equipment	20 years
Logging machinery and equipment	5 to 7 years
Other manufacturing machinery and equipment	7 to 13 years
Tugs, barges and scows	10 to 13 years

(f) Intangible assets –

The unallocated purchase price of shares in subsidiaries as at January 1, 1978 is being amortized on a straight-line basis over a period of twenty years.

Amortization of financing expenses relating to bonds and debentures is computed on a basis related to the principal amounts outstanding over the terms of the issues.

(g) Income taxes –

Income taxes are recorded on a tax allocation basis. Accordingly, deferred income tax provisions (or reductions) are recorded in the statements of earnings in appropriate amounts to reflect the income tax effects of timing differences arising each year. In MacMillan Bloedel's case, such differences have resulted principally from depreciation being claimed for income tax purposes in amounts differing from depreciation recorded for accounting purposes.

Investment tax credits are accounted for as a reduction of current and deferred income tax expense.

(h) Pension costs –

Normal pension cost accruals are made on the basis of annual reviews of the position of MacMillan Bloedel's various pension plans and other retirement arrangements. Pension plan surpluses and deficits are amortized to earnings over appropriate periods. Past service pension costs arising from plan amendments in 1979 (Note 14) are being charged to earnings over a period of fifteen years.

(i) Capitalized interest –

Interest charges are allocated between major capital projects during their construction phase and interest expense.

2. Accounting change:

Commencing with 1980 MacMillan Bloedel changed its method of calculating depreciation on manufacturing assets from a straight-line basis to a units-of-production basis. Had this method been used in 1979, the effect would have been to increase net earnings by approximately \$300,000 (\$.01 per Common share).

3. Inventories:

	1981	December 31 1980
	(\$'000)	
Operating and maintenance supplies	\$ 63,107	\$ 57,579
Logs, poles, pulp chips, pulpwood and cordwood	137,529	152,262
Lumber, plywood and other building materials	123,799	145,408
Pulp and paper products	33,905	24,775
Containerboard and packaging products	58,601	42,916
	\$416,941	\$422,940

Approximately \$91,000,000 of lumber and certain other building materials are valued at net realizable value.

4. Partly-owned companies:

	December 31	
	1981	1980
	(\$'000)	
Investments	\$39,518	\$38,296
Accumulated equity in undistributed earnings since acquisition, less allowance for possible loss of \$2,100,000 (1980-\$2,358,000)	27,062	30,557
	\$66,580	\$68,853

The above amounts include \$49,963,000 at December 31, 1981 (1980 – \$49,923,000) in respect of Koninklijke Nederlandse Papierfabrieken N.V., a paper and packaging company based in The Netherlands in which MacMillan Bloedel has a 48.0% interest. Summarized consolidated financial information for this company as at December 31, 1981 and 1980 and for the three years ended December 31, 1981 is as follows:

	December 31	
	1981	1980
	(\$'000)	
Assets	\$334,803	\$306,051
Liabilities	\$220,850	\$189,477
Shareholders' equity	113,953	116,574
	\$334,803	\$306,051

	Year ended December 31		
	1981	1980	1979
	(\$'000)		
Sales and other income	\$567,900	\$626,396	\$565,301
Net earnings (loss)*	\$ (2,621)	\$ 1,343	\$ 5,518
MacMillan Bloedel's share in net earnings (loss) for the year (after consolidating adjustments)	\$ (1,320)	\$ (99)	\$ 893

*After provisions for losses of \$8,700,000 in 1980, and \$16,400,000 in 1979, in respect of certain old and uneconomic paper machines and a boxboard plant. MacMillan Bloedel's share of these losses amounted to \$4,000,000 in 1980 and \$7,000,000 in 1979.

5. Buildings and equipment:

	Cost*	Accumulated depreciation	Net
	(\$'000)		
December 31, 1981 –			
Raw materials and building materials	\$ 529,015	\$ 265,470	\$ 263,545
Pulp and paper	934,960	390,060	544,893
Containerboard and packaging	381,729	109,016	272,713
Other	8,701	6,145	2,556
Corporate assets	50,150	14,801	35,349
	\$1,904,548	\$ 785,492	\$1,119,056
December 31, 1980** –			
Raw materials and building materials	\$ 507,229	\$ 246,483	\$ 260,746
Pulp and paper	934,960	400,525	534,435
Containerboard and packaging	251,762	98,295	153,467
Other	8,855	5,718	3,137
Corporate assets	39,894	13,143	26,751
	\$1,742,700	\$ 764,164	\$ 978,536

*Includes construction in progress.

**Certain 1980 amounts have been reclassified to agree with the presentation in 1981.

Assets aggregating \$124,178,000 (1980 – \$90,779,000) (mainly the Alabama facilities) and the related depreciation and long term debt are included in the accompanying financial statements as they are held under capital leases.

Capital Expenditure Program:

MacMillan Bloedel has substantially reduced its capital expenditure program pending an improvement in economic conditions. Of the major projects in progress at December 31, 1981

the Pine Hill, Alabama expansion program is proceeding as planned and has a total estimated cost of \$355,000,000. Completion of the Nanaimo, B.C. recovery boiler and the Annacis Island, B.C. paper machine projects has been deferred.

	Costs included in construction in progress at December 31, 1981	Construction commitments at December 31, 1981
Pine Hill expansion program	\$122,601,000	\$ 43,804,000
Recovery boiler	7,649,000	40,755,000
Fine paper machine	28,874,000	6,234,000
	\$159,124,000	\$ 90,793,000

6. Short term bank indebtedness and bank lines of credit:

At December 31, 1981 MacMillan Bloedel had short term bank lines of credit aggregating \$294,749,000 (1980 – \$171,556,000). At December 31, 1981 \$94,116,000 (1980 – \$54,081,000) of these short term bank lines had been drawn down.

7.(a) Bonds and debentures:

	December 31	
	1981	1980
	(\$'000)	
MacMillan Bloedel Limited –		
4.95%* sinking fund debentures, Series A, maturing October 1, 1990 (U.S. \$18,900,000)	\$ 20,304	\$ 22,560
6½% sinking fund debentures, Series C, maturing July 15, 1992 (U.S. \$14,870,000)	16,025	17,760
8½% sinking fund debentures, Series E, maturing May 15, 1991	14,864	15,628
8½% sinking fund debentures, Series F, maturing July 1, 1994 (U.S. \$61,500,000)	59,351	63,701
11½% sinking fund debentures, Series G, maturing January 15, 1995	35,916	37,928
9% sinking fund debentures, Series J, maturing February 1, 1992 (U.S. \$42,737,000)	43,581	45,073
9¼% sinking fund debentures, Series K, maturing March 15, 1993 (U.S. \$43,256,000)	47,736	49,715
8½% subordinated debentures, maturing December 20, 1984 (U.S. \$2,098,000)	2,075	2,075
	239,852	254,440

MacMillan Bloedel Inc.** –

4½% sinking fund industrial development revenue bonds, maturing June 1, 1988 (U.S. \$27,740,000)	29,821	37,216
4.90% – 5.50% general obligation industrial bonds, series 1977, maturing December 1, 1997 (U.S. \$820,000)	872	894
8¼% pollution control bonds, maturing November 1, 1983 (U.S. \$32,000,000)	38,480	38,480
10¼% pollution control bonds, maturing November 1, 2000 (U.S. \$15,000,000)	18,038	18,038
10½% pollution control bonds, maturing November 1, 2015 (U.S. \$15,000,000)	18,038	18,038
8¼% environmental improvement bonds, maturing November 1, 1983 (U.S. \$1,000,000)	1,202	1,202
8¼% industrial development bonds, maturing November 1, 1983 (U.S. \$425,000)	511	511
8¼% industrial development revenue bonds, maturing November 1, 1983 (U.S. \$1,700,000)	2,044	2,044
11½% to 11¼% (9½% from March, 1982) industrial development revenue bond, maturing in 1987 (U.S. \$10,509,000)	12,652	—
	121,658	116,423

7.(a) Bonds and debentures: continued

MacMillan Rothesay Limited –

6% first mortgage and collateral sinking fund bonds, Series A, maturing March 1, 1985	\$ —	\$ 4,526
6% general mortgage sinking fund bonds, Series A, maturing October 1, 1985	—	2,905
	—	7,431
	361,510	378,294
Less: Payments due within one year, before adjustment to current rate of exchange (Notes 1(b) and 9)	8,129	10,991
	\$353,381	\$367,303

*Extra interest of ½ of 1% per year has been paid on these debentures from January 1, 1975 consequent upon amendment of the relevant trust indenture.

**The bonds listed under MacMillan Bloedel Inc. are direct obligations of Industrial Development Boards and municipal authorities in Alabama and Mississippi.

Substantially all of MacMillan Bloedel's assets are pledged by fixed and floating charges as security for the outstanding debentures and other liabilities. The trust indentures securing the Company's debentures contain provisions limiting the amount of indebtedness which the Company can incur and limiting the amount of dividends. At December 31, 1981, approximately \$220,000,000 of additional long term indebtedness and an unlimited amount of short term indebtedness could be incurred; approximately \$470,000,000 was available for payment of dividends. These amounts would be reduced by any redemption of shares (Note 10).

Long term debt repayable in foreign currencies has been translated into Canadian dollars at historical exchange rates (Note 1(b)). At December 31, 1981 there were unrealized losses on foreign exchange relating to long term debt of approximately \$19,870,000 which have not been recognized in the accompanying financial statements. The exchange ratio between the applicable foreign currencies and the Canadian dollar will be subject to many fluctuations during the time to maturity of the long term debt.

(b) Funds held for construction projects:

Unexpended funds, including income, from the municipal bonds issued in 1980 and listed under MacMillan Bloedel Inc. are shown as "Funds held for construction projects" on the balance sheet. Pursuant to the terms of issue, the funds may only be expended on specific capital projects at Pine Hill, Alabama and accordingly the \$74,351,000 shown on the balance sheet will be drawn down as construction progresses.

8. Term bank loans and bank lines of credit:

	December 31	
	1981	1980
		(\$000)
Unsecured term bank loan of U.S. \$50,000,000 maturing September 30, 1990 bearing interest at a floating rate not to be less than 9% nor greater than 12½%	\$ 58,788	\$ 58,788
Unsecured term bank loan of 60,000,000 Dutch guilders maturing January 15, 1993 bearing interest at 11½%	33,983	33,983
Unsecured term bank loan of U.S. \$6,915,240 maturing in 1989 bearing interest at 11¼% to 11¾% (from June, 1982 interest will be in part at 9¼% and in part at a rate related to the London Interbank rate for U.S. dollar deposits.)	8,280	—
Unsecured term bank loan of 40,000,000 Dutch guilders maturing January 15, 1992 bearing interest at 12½%	19,303	—
Advances under contractual term lines of credit (including advances of £10,000,000 and U.S. \$10,000,000, (1980 – £8,000,000))	103,855	67,380
	224,209	160,151
Less: Payments due within one year, before adjustment to current rate of exchange (Notes 1(b) and 9)	482	—
	\$223,727	\$160,151

At December 31, 1981 MacMillan Bloedel had contractual term bank lines of credit aggregating \$593,300,000 (1980 – \$358,230,000). At December 31, 1981 \$103,855,000 (1980 – \$67,380,000) of these term bank lines had been drawn down. These contractual term lines provide for unsecured loans on a revolving basis during the first three or five years, followed by a seven or ten year repayment period.

9. Payments on long term debt:

Payments on long term debt required for each of the five years after December 31, 1981 are as follows –

	Bonds and debentures	Term bank loans	Other liabilities	Total
			(\$000)	
1982 (after adjustment to current rate of exchange – Notes 1(b) and 7(a))	\$ 9,543*	\$ 483	\$8,775	\$18,801
1983	63,198*	965	1,581	65,744
1984	23,630	2,853	1,648	28,131
1985	21,760	7,112	1,527	30,399
1986	21,969	7,112	1,644	30,725

*Net of purchases and cancellation of bonds and debentures to December 31, 1981.

10. Share capital:

By resolution of the shareholders passed on June 25, 1981 the Company's authorized capital was increased from 35,000,000 Common shares, 3,400,000 Class A Preferred shares, and 5,000,000 Class B Preferred shares issuable in series, all without par value to 35,000,000 Common shares, 3,400,000 Class A Preferred shares and 8,000,000 Class B Preferred shares issuable in series, all without par value, and provided that the Class B Preferred shares shall not be issued for an aggregate consideration in excess of \$200 million.

The following is a summary of the changes in share capital since January 1, 1979:

	Issued	
	Number of shares	(\$000)
Class A Preferred shares		
Balance January 1, 1979		
unchanged to December 31, 1981	3,400,000	\$ 87,954
Class B Preferred shares		
Series 1		
Issued in 1980 and outstanding at December 31, 1980	2,000,000	\$ 50,000
Converted to 98,323 Common shares during 1981	(151,530)	(3,788)
Balance December 31, 1981	1,848,470	\$ 46,212
Series 2		
Issued in 1981	2,000,000	\$ 50,000
Converted to 7,375 Common shares during 1981	(13,300)	(332)
Balance December 31, 1981	1,986,700	\$ 49,668
Series 3		
Issued in 1981 and outstanding at December 31, 1981	280,000	\$ 28,000
Common shares		
Balance January 1, 1979	21,261,175	\$171,175
Share options exercised, 1979	11,800	240
Balance December 31, 1979, and 1980	21,272,975	171,415
Share options exercised	5,000	101
Senior management share purchase plan	35,520	1,513
Conversion of Class B Preferred shares	105,698	4,115
Balance December 31, 1981	21,419,193	\$177,144

The Class A Preferred shares are redeemable, at the option of the Company, on or after May 1, 1982 at U.S. \$25.00 per share; the shares are retractable, at the option of the holder, on May 1, 1987 at U.S. \$25.00 per share. The shares carry the right to cumulative preferential dividends of 5¼% per annum to May 1, 1982 and thereafter at a rate of 1 ½% above one-half of the average U.S. prime rate.

The Class B Preferred shares:

Series 1

Each of these Convertible Preferred shares is convertible into Common shares of the Company at any time on or before December 1, 1985 at a conversion price of \$38.50 per Common share, and thereafter and on or before December 1, 1990 at a conversion price of \$40.50 per Common share. As at December 31, 1981, the Company has reserved 1,200,378 Common shares for possible issuance upon the exercise of this conversion privilege. The Convertible Preferred shares, Series 1, are not redeemable on or prior to August 31, 1983 and are redeemable thereafter on or prior to September 1, 1985 only if the weighted average price at which the Common shares traded in a specified period was not less than 125% of the conversion price applicable at the time. After September 1, 1985 the Convertible Preferred shares, Series 1, are redeemable at \$25.00 per share plus a redemption premium of \$1.25 per share declining annually by \$.25. The Company is required to make all reasonable efforts to purchase during each calendar quarter (cumulative during the year), commencing January 1, 1991, at a price not exceeding \$25.00 per share, 1% of the number of Convertible Preferred shares outstanding on December 2, 1990. The shares carry the right to cumulative preferential dividends of \$2.00 per annum, payable quarterly.

Series 2

Each of these Convertible Preferred shares is convertible into Common shares of the Company at any time on or before March 1, 1986 at a conversion price of \$45.00 per Common share, and thereafter and on or before March 1, 1991 at a conversion price of \$49.00 per Common share. As at December 31, 1981, the Company has reserved 1,103,736 Common shares for possible issuance upon the exercise of this conversion privilege. The Convertible Preferred shares, Series 2, are not redeemable on or prior to February 29, 1984 and are redeemable thereafter on or prior to March 1, 1986 only if the weighted average price at which the Common shares traded in a specified period was not less than 125% of the conversion price applicable at the time. After March 1, 1986 the Convertible Preferred shares, Series 2, are redeemable at \$25.00 per share plus a redemption premium of \$1.25 per share declining annually by \$.25. The Company is required to make all reasonable efforts to purchase during each calendar quarter (cumulative during the year), commencing April 1, 1991, at a price not exceeding \$25.00 per share, 1% of the number of Convertible Preferred shares outstanding on March 2, 1991. The shares carry the right to cumulative preferential dividends of \$2.08 per annum, payable quarterly.

Series 3

The Company shall, during March in each of the years 1982 through 1985 inclusive offer to redeem 5% of each holder's original holdings at a price per share of \$100 and on July 1 in each of the years 1986 through 1990 shall redeem 5% of each holder's original holdings at a price of \$100 per share. On July 1, 1991 the Company shall redeem all the Preferred shares, Series 3, outstanding at a price per share of \$100. After July 1, 1985 the Preferred shares, Series 3, are redeemable at \$100 per share plus a redemption premium of \$3.00 per share declining annually by \$.50. The shares carry the right to cumulative preferential dividends equal to the sum of 1¼% and ½ of the defined Average Minimum Lending Rate.

The Class B Preferred shares rank on a parity with the Class A Preferred shares and prior to the Common shares of the Company.

Options for Common shares may be granted to key employees, exercisable on or before dates fixed by the Board of Directors. Options for 11,800 shares were exercised in 1979. Options for 57,300 shares at \$20.30 per share were relinquished in 1979 (Note 13(a)). An option for 1,000 shares was granted and an option for 5,000 shares was exercised in 1981, leaving the outstanding options at December 31, 1981 as follows:

Number of shares	Option price	Expiry date
50,000 shares	\$19.69	August 31, 1986
1,000 shares	\$42.59	June 24, 1991

At December 31, 1981 loans to senior officers under the Senior Management Share Purchase Plan amounted to \$1,256,000. The majority of the loans are non-recourse, interest free, for a ten year term and secured by a pledge of the Common shares.

11. Commitments:

In addition to commitments for capital expenditures and the future supply of operating services and materials, MacMillan Bloedel is committed in respect of the following –

- (a) Ship charters and rentals under non-cancellable leases having an initial term of more than one year as follows –

	Ship Charters	Leases	Total
		(\$000)	
1982	\$ 40,546	\$ 7,400	\$ 47,946
1983	40,573	5,832	46,405
1984	34,310	4,462	38,712
1985	18,020	3,191	21,211
1986	9,976	2,124	12,100
1987-1991	14,531	4,200	18,731
1992-1996	—	3,474	3,474
1997-2001	—	2,992	2,992
Subsequent to 2001	—	6,748	6,748
	\$157,956	\$40,363	\$198,319

Ship charter commitments payable in foreign currencies, including a major portion in Deutsche marks, have been translated into Canadian dollars at exchange rates prevailing at December 31, 1981.

As at December 31, 1981 some of the ship charters are at rates above those prevailing in the spot charter market at that date.

- (b) The acquisition of timber in Alabama under long term cutting contracts requiring minimum annual payments (extending in some cases to the year 2034); payment of approximately \$4,657,000 is required in each of the next five years.

- (c) The sale under forward exchange contracts of U.S. \$333,730,000 during 1982 at rates averaging approximately Canadian \$1.2221 for each United States \$1.00. The spot rate at December 31, 1981 was Canadian \$1.1866 for each United States \$1.00.

12. Contingent liabilities:

MacMillan Bloedel is subject to a number of investigations, claims and legal proceedings, all of which are of an ordinary routine nature incidental to its business. MacMillan Bloedel considers its provisions for such claims and legal proceedings are adequate on the basis of current information.

13. Earnings statements supplementary information:

(a) Costs and expenses include the following –

	Year ended December 31		
	1981	1980 (\$000)	1979
Interest expense –			
Long term debt interest	\$66,346	\$36,023	\$30,430
Other interest	10,116	10,377	2,248
	76,462	46,400	32,678
Less: Interest capitalized	13,285	14,543	3,800
	\$63,177	\$31,857	\$28,878
Depreciation (Note 2)	\$74,117	\$71,840	\$65,618
Depletion	12,839	10,255	9,420
Logging road amortization	5,009	6,637	7,548
	\$91,965	\$88,732	\$82,586
Pension expense	\$42,396	\$38,603	\$30,575
Research and development expenses (net of government grants of \$368,000 in 1981, 1980 – \$543,000, 1979 – \$510,000).	\$ 9,378	\$ 8,169	\$ 7,128
Rental expense on leases of more than one month, and time charter hire.	\$49,501	\$47,261	\$42,623

Selling, general and administrative expenses include direct remuneration of the directors and senior officers of the Company aggregating \$3,570,000 (1980 – \$4,102,000; 1979 – \$4,463,000). The 1979 amount includes payments upon relinquishment of stock options (Note 10) and the 1979 and 1980 amounts include compensation under a Management Incentive Compensation Plan.

(b) Income taxes –

Consolidated income tax expense (recovery) is composed of –

	Canadian federal	Canadian provincial	Foreign	Total
Year ended December 31, 1981				
Current	\$ 775	\$ (1,007)	\$ 7,852	\$ 7,620
Deferred	(15,828)	(12,766)	(10,352)	(38,946)
	\$ (15,053)	\$ (13,773)	\$ (2,500)	\$ (31,326)
Year ended December 31, 1980				
Current	\$ (656)	\$ (912)	\$ 8,783	\$ 7,215
Deferred	23,624	23,255	8,874	55,753
	\$ 22,968	\$ 22,343	\$ 17,657	\$ 62,968
Year ended December 31, 1979				
Current	\$ 32,669	\$ 27,941	\$ 3,295	\$ 63,905
Deferred	17,280	11,043	8,143	36,466
	\$ 49,949	\$ 38,984	\$ 11,438	\$100,371

Deferred income taxes result from timing differences in the recognition of revenue and expense for tax and financial statement purposes. The sources of these differences and the tax effects of each were as follows:

	Year ended December 31		
	1981	1980 (\$000)	1979
Deferred income taxes –			
Excess of income tax allowances over financial statement depreciation and logging road amortization	\$(18,481)	\$53,919	\$35,409
Inventory valuation for financial statement purposes over valuation for income tax purposes	9,129	4,220	1,397
Provision for withholding taxes on undistributed earnings of foreign subsidiaries	(2,500)	1,737	300
Expense provisions not deductible for income tax purposes until paid	(15,636)	1,643	4,728
Non-capital losses for which deferred tax allocation was followed	(13,116)	3,081	(2,409)
United States and Canadian investment tax credits	(2,897)	(5,350)	(4,492)
United Kingdom stock appreciation relief	—	(5,265)	2,461
Imputed interest on Alabama timberlands	(1,302)	1,838	378
Rental on Alabama timberlands	5,160	263	1,527
Other items which are individually less than 5% of computed "expected" income taxes	697	(333)	(2,833)
	\$(38,946)	\$55,753	\$36,466

MacMillan Bloedel's effective income tax rates for 1981, 1980 and 1979 are determined as follows:

	Year ended December 31		
	1981	1980	1979
Canadian federal income tax rate	(46.0)%	46.0%	46.0%
Canadian manufacturing and processing allowance	5.7	(3.2)	(3.5)
Provincial income and logging taxes, and State taxes and withholding tax provisions net of applicable federal abatements	(7.1)	4.9	4.5
Operating and capital losses for which potential tax reductions were not recorded	(1.1)	(2.0)	—
Investment tax credits	(17.4)	(4.4)	(3.7)
3% Canadian inventory allowance	(7.9)	(1.8)	(1.0)
United Kingdom stock appreciation relief	(2.3)	(1.4)	(1.0)
Effect of foreign exchange translation adjustments	(1.6)	(1.1)	(.4)
Effect of low rate of tax on capital gains	(.5)	(1.5)	(1.4)
Effect of recording tax adjustments and assessments	12.4	(1.3)	.3
Other items	3.1	.7	(.7)
Effective income tax rate	(62.7)%	34.9%	39.1%

Certain subsidiary companies have losses aggregating \$19,533,000 available for carry forward to reduce income taxes which may become payable in future years. The potential tax benefit of these losses has not been reflected in these financial statements.

(c) Extraordinary item –

Effective July 28, 1981 the Company sold its 65% interest in MacMillan Rothesay Limited, a manufacturer of newsprint located in St. John, New Brunswick. The Company realized a profit on disposal of \$29,997,000 (net of income taxes of \$9,200,000) as a result of the transaction.

(d) Net earnings per Common share –

Net earnings per Common share is computed by dividing the net earnings, after providing for dividends on the Class A and Class B Preferred shares, by the weighted average number of Common shares outstanding during the year.

There would have been no increase in the net loss per Common share in 1981 from the conversion of outstanding convertible securities.

14. Pension plans:

MacMillan Bloedel has a number of contributory and non-contributory pension plans, participation in which is available to substantially all employees after one or two years of continuous service. In addition, the Company has agreements with a number of its officers and executives (including some now retired) which call for payments to be made under certain conditions following retirement. Pension and retirement benefits are determined as a function of service and earnings.

Contributions to plan funds are made pursuant to actuarial recommendations.

At December 31, 1981 the obligations for pension benefits under all plans and obligations under other unfunded agreements exceeded the total of the pension fund assets and the balance sheet provisions for pension obligations by approximately \$14,100,000. The obligations at December 31, 1981 include past service pension obligations arising from plan amendments in 1979 (estimated at \$26,000,000 at the end of that year). The unamortized past service pension obligations are to be charged to earnings over the ensuing 13 years of the amortization period.

	December 31 1981	1980
	(\$000)	
Obligations for pension benefits under all plans and agreements	\$306,700	\$282,900
Plan assets	265,400	268,500
Unfunded obligations	41,300	14,400
Balance sheet provisions	27,200	17,800
Net surplus (deficiency)	\$ (14,100)	\$ 3,400

15. Segment information:

Information concerning MacMillan Bloedel's business on a segmented basis is set out in Exhibits I and II attached.

16. Information with respect to generally accepted accounting principles in the United States:

(a) Effect of United States accounting principles on net earnings –

As disclosed in Note 1, the attached financial statements are prepared in accordance with accounting principles generally accepted in Canada. These accounting principles differ from those generally accepted in the United States. In MacMillan Bloedel's case the principal difference relates to the methods of translating amounts denominated in foreign currencies including the financial statements of foreign subsidiaries (Note 1(b)). MacMillan Bloedel has based its calculations upon Financial Accounting Standards Statement no. 8 for accounting principles generally accepted in the United States. Had accounting principles generally accepted in the United States been followed in the preparation of these financial statements, consolidated net earnings for 1981 would have been increased by approximately \$41,000,000 (\$1.92 per Common share), and reduced in 1980 by \$5,000,000 (\$.24 per Common share), and increased in 1979 by \$15,000,000 (\$.71 per Common share).

(b) Shareholders' equity –

As at December 31, 1981 shareholders' equity as shown in the balance sheet would have amounted to \$746,216,000 (1980 – \$737,352,000) had the preferred shares been shown separately as required by rules of the United States Securities and Exchange Commission and the retained earnings adjusted for the effect of United States accounting principles in (a) above.

17. Subsidiary companies:

Active

Canada

Canadian Transport Company Limited
Canadian Transport (Europe) Limited
Forest Industries Flying Tankers Limited
MacMillan Bloedel Building Limited
MacMillan Bloedel Industries Limited (1)
MacMillan Bloedel Packaging Limited
MacMillan Bloedel Properties Limited
Vancouver Marine Engines Ltd.

United States

Atlantic Forest Products Inc.
Canadian Transport (N.Y.) Inc.
Fibres International, Inc.
MacMillan Bloedel Export Inc.
MacMillan Bloedel Inc.
MacMillan Bloedel Particleboard Inc.
Powell River-Alberni Sales Corporation
Star Terminal Company, Incorporated

United Kingdom

Canadian Transport (Terminals) Limited
MacMillan Bloedel Containers Limited
MacMillan Bloedel Meyer Limited
MacMillan Bloedel Meyer (Terminals) Limited
MacMillan Bloedel Panelboard Agencies Limited
MacMillan Bloedel Pulp and Paper Sales Limited
Pakfast Limited
Scotpack Limited

Other

Altair Limited (2)
Comfloresta-Companhia Catarinense de
Empreendimentos Florestais (3)
Embrasca-Empreendimentos Florestais e
Agrícolas Ltda. (3)
Fortrans N.V.
MacMillan Bloedel Europe B.V.
MacMillan Bloedel Pty. Limited
MacMillan Jardine (Japan) Limited
MacMillan Jardine Limited
MacMillan Jardine (South East Asia) Limited

Inactive (including holding companies not carrying on active operations)

Harmac Ltd.
Kingcome Navigation Company Ltd.
MacMillan Bloedel Canadian Holdings Limited
MacMillan Bloedel Export Sales Ltd.
MacMillan Bloedel (Saskatchewan) Limited
Powell River-Alberni Sales Limited
Vancouver Island Sievedoring Co. Ltd.
231267 B.C. Ltd.

MB Subsidiary 74 Inc.
MacMillan Bloedel Radio System, Inc.
MacMillan Bloedel Timberlands Inc.

Hygrade Corrugated Cases Limited
MacMillan Bloedel Holdings (U.K.) Limited

Canadian Maas River Investment N.V.
Canadian Transport Company Pty. Limited
Canadian Transport (Orient) Limited
Comfloresta-Parana Empreendimentos
Florestais S.A. (3)
Comfloresta-Serrana Empreendimentos
Florestais S.A. (3)
Island Risk Management Limited
MacMillan Bloedel (Brasil) Ltda.
MacMillan Bloedel European Holdings B.V.
MacMillan Bloedel Holding N.V.
MacMillan Jardine (Malaysia) Sendirian Berhad
MB Bermuda Limited
Oceanspan Carriers Limited

(1) Merged with MacMillan Bloedel Limited after the close of business on December 31, 1981.

(2) November 30 year-end for fiscal purposes.

(3) These companies are accounted for by the equity method.

Segment Information

Earnings Statements

Exhibit I	Sales of products and services (2) Year ended December 31			Contributions to earnings (3) Year ended December 31		
	1981	1980	1979	1981	1980*	1979
	(\$ millions)			(\$ millions)		
Raw materials and building materials	\$ 946.9	\$1,156.7	\$1,176.5	\$ (82.2)	\$ 56.9	\$155.4
Pulp and paper	830.9	914.9	672.4	92.1	131.2	122.5
Containerboard and packaging	524.5	515.1	414.0	31.4	38.5	26.9
Other	33.2	29.6	32.5	.9	1.1	1.4
	2,335.5	2,616.3	2,295.4	42.2	227.7	306.2
Add (deduct): Inter-segment eliminations	(125.8)	(179.9)	(115.1)	2.4	(.1)	(4.6)
Sales/ Operating earnings	\$2,209.7	\$2,436.4	\$2,180.3	\$ 44.6	\$227.6	\$301.6
Sales of products and services:						
Canada – Domestic	\$ 530.8	\$ 494.9	\$ 409.4			
United States	546.8	591.6	590.0			
Europe	207.1	351.3	303.4			
Other	363.0	436.5	316.8			
	1,647.7	1,874.3	1,619.6	\$ 18.2	\$187.7	\$268.3
United States	856.1	846.1	878.9	22.3	27.9	10.1
Europe (primarily the United Kingdom)	202.5	235.3	201.6	(1.1)	2.7	17.1
Other	6.0	5.2	4.9	.7	3.3	5.6
	2,712.3	2,960.9	2,705.0	40.1	221.6	301.1
Add (deduct): Inter-area eliminations	(502.6)	(524.5)	(524.7)	4.5	6.0	.5
Sales/ Operating earnings	\$2,209.7	\$2,436.4	\$2,180.3	\$ 44.6	\$227.6	\$301.6
Operating earnings				\$ 44.6	\$227.6	\$301.6
Deduct: Unallocated general and administrative expenses				53.0	41.9	37.9
Interest expense				63.2	31.9	28.9
Corporate (gains) and losses and investment income				(21.7)	(26.4)	(22.2)
				94.5	47.4	44.6
Earnings (loss) before income taxes, equity in earnings of partly-owned companies, minority interests in subsidiaries and extraordinary item				\$ (49.9)	\$180.2	\$257.0

* Certain 1980 amounts have been reclassified.

(1) Basis of segmentation -

MacMillan Bloedel carries on an integrated forest products business which involves extensive transfers of raw materials and products among operations. Accordingly, segmentation of the business by product and service categories involves allocating conversion and other costs and establishing transfer pricing policies for joint raw materials and other products. Under the policy followed by MacMillan Bloedel, inter-segment transfers of products, including logs and wood chips transferred from the raw materials and building materials segment to the pulp and paper segment, are made at market values. Costs are allocated on a basis which MacMillan Bloedel believes to be reasonable. However, other pricing policies and methods of allocating costs are possible.

(2) Sales of products and services -

Sales of the raw materials and building materials segment exclude the proceeds of log sales and trades with third parties resulting from the need to match logs produced with the requirements of the converting mills. Such proceeds are credited against production costs. Sales of the raw materials and building materials segment include the proceeds of logs and chips transferred to the pulp and paper segment.

(3) Contributions to earnings -

Contributions to earnings represent sales of products and services less cost of sales and services, selling expenses and allocated general and administrative expenses.

Exhibit II

Exhibit II	December 31		
	1981	1980	
Segment assets:	(\$ millions)		
Raw materials and building materials	\$ 738.8	\$ 766.4	
Pulp and paper	738.2	751.4	
Containerboard and packaging	506.0	381.0	
Other	7.9	8.1	
	1,990.9	1,906.9	
Add: Inter-segment eliminations	5.0	2.6	
	\$1,995.9	\$1,909.5	
Segment assets:			
Canada	\$1,325.0	\$1,363.6	
United States	557.8	424.5	
Europe (primarily the United Kingdom)	110.6	122.6	
Other	3.8	4.6	
	1,997.2	1,915.3	
Less: Inter-area eliminations	1.3	5.8	
	\$1,995.9	\$1,909.5	
Reconciliation with consolidated assets:			
Segment assets	\$1,995.9	\$1,909.5	
Partly-owned companies	66.6	68.9	
Other corporate assets	109.6	96.8	
Consolidated assets	\$2,172.1	\$2,075.2	
	Year ended December 31		
	1981	1980	1979
Additions to property, plant and equipment:	(\$ millions)		
Raw materials and building materials	\$ 58.2	\$ 88.4	\$119.4
Pulp and paper	105.3	183.0	118.3
Containerboard and packaging	133.2	47.5	36.8
Other	—	1.0	.1
	296.7	319.9	274.6
Corporate assets	11.2	7.8	5.8
	\$307.9	\$327.7	\$280.4
Depreciation, depletion and logging road amortization:			
Raw materials and building materials	\$ 44.4	\$ 45.9	\$ 45.5
Pulp and paper	31.4	28.5	24.5
Containerboard and packaging	13.1	11.2	9.8
Other	.6	.7	1.2
	89.5	86.3	81.0
Corporate assets	2.5	2.4	1.6
	\$ 92.0	\$ 88.7	\$ 82.6

Segment Information

Balance Sheets

Segment Statistics

Containerboard and Packaging

Containerboard and Packaging Facilities

Location	Aggregate effective annual capacities	1981 Production
thousand tonnes		
Linerboard		
Pine Hill, Ala.	354	311
Port Alberni, B.C.	110	52
	464	363
Corrugating Medium		
Sturgeon Falls, Ont.	71	68
Bags		
Vancouver, B.C.	14	11

Sales of Containerboard and Packaging Products (\$ millions)

	1977	1978	1979	1980	1981
Corrugated Containers	\$218.4	\$250.9	\$308.1	\$374.3	\$391.0
Containerboard	72.0	81.4	90.6	116.1	115.0
Bags	5.7	7.3	8.6	9.9	10.9
Other	11.4	12.8	6.7	14.8	7.6
Total Segment Sales	\$307.5	\$352.4	\$414.0	\$515.1	\$524.5
Segment Contribution to Operating Earnings	\$ 18.8	\$ 17.5	\$ 26.9	\$ 38.5	\$ 31.4

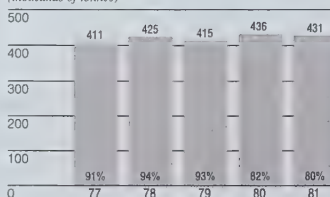
Containerboard and Packaging Segment Sales by Market in 1981

	Containerboard	Bags (thousand tonnes)	Corrugated Containers
North America	219	11	329
Overseas	59	—	99
Total	278	11	428

Containerboard and Packaging Production

Containerboard

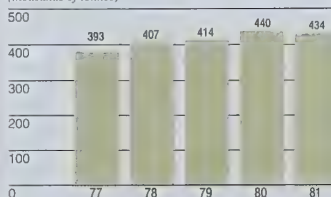
(thousands of tonnes)



Percentage figures are average annual operating rates

Corrugated Containers

(thousands of tonnes)



Corrugated Containers

Canada: 156,000 tonnes production in 1981

Montreal, Que. • Pembroke, Ont. • Rexdale, Ont. • Guelph, Ont. • London, Ont. • Winnipeg, Man. • Regina, Sask. • Edmonton, Alta. • Calgary, Alta. • New Westminster, B.C.

United States: 176,000 tonnes production in 1981

Elmira, NY • Jersey City, NJ • Union, NJ • Odenton, MD • Cleveland, OH • Chicago, IL • Little Rock, AR • Magnolia, MS • Houston, TX

United Kingdom: 102,000 tonnes production in 1981

Hatfield, Hertfordshire • Southall, Hanwell • West Auckland, Durham • Nelson, Lancashire • Weston-super-Mare, Avon • Irvine, Ayrshire

Sales of Pulp and Paper Products (\$ millions)

	1977	1978	1979	1980	1981
Newsprint	\$385.7	\$463.2	\$425.7	\$586.4	\$559.6
Market Pulp	143.9	161.3	181.7	246.6	207.0
Fine Papers	22.4	25.9	29.6	35.7	35.4
Recycled Fibre and other	24.2	22.1	35.4	46.2	28.9
Total Segment Sales	\$576.2	\$672.5	\$672.4	\$914.9	\$830.9
Segment Contribution to Operating Earnings	\$116.7	\$137.5	\$122.5	\$131.2	\$ 92.1

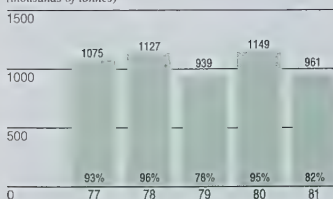
Pulp and Paper Segment Sales by Market in 1981 (thousand tonnes)

	Newsprint	Market Pulp	Fine Papers	Recycled Fibre
British Columbia	62	—	23	1
Rest of Canada	46	—	10	6
United States	643	45	—	78
Japan and Orient	78	97	—	—
United Kingdom and Europe	16	168	—	—
Other	112	16	—	—
Total	957	326	33	85

Pulp and Paper Production

Newsprint

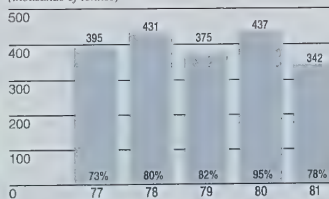
(thousands of tonnes)



Percentage figures are average annual operating rates

Market Pulp

(thousands of tonnes)



Pulp and Paper Distribution Centres

Australia: MacMillan Bloedel Pty. Limited, Sydney

Canada: MacMillan Bloedel Limited, Vancouver, B.C.

Orient: MacMillan Jardine Limited, Hong Kong · Japan · Malaysia

United Kingdom and Europe: MacMillan Bloedel Europe B.V., Brussels, Belgium
MacMillan Bloedel Pulp and Paper Sales Limited, London, England

United States: MacMillan Bloedel Inc., Stamford, CT · Powell River-Alberni Sales Corporation, Seattle, WA · San Bruno · Pasadena, CA · Star Terminal Company Incorporated, San Francisco · Long Beach, CA

Segment Statistics

Pulp and Paper

Pulp and Paper Facilities

Location	Aggregate effective annual capacities	1981 Production
Newsprint, including Groundwood Specialties (thousand tonnes)		
Powell River, B.C.	670	493
Port Alberni, B.C.	380	283
	1,050	776

Market Pulp

Nanaimo, B.C.	340	274
Port Alberni, B.C.	56	44
Powell River, B.C.	24	24
	420	342

Fine Papers

New Westminster, B.C.	38	34
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Segment Statistics

Raw Materials and Building Materials

Building Materials Facilities

Location	Aggregate effective annual capacities	1981 Production
Lumber	MMFBM	
Port Alberni, B.C.*	506	256
Nanaimo, B.C.	342	173
Vancouver, B.C.	248	164
Chemainus, B.C.	242	135
New Westminster, B.C.*	104	51
Powell River, B.C.	80	57
Pine Hill, Ala.	75	59
Edmonton, N.C.*	15	15
	1,612	910

*Lumber specialty mills at these locations

Plywood	MM sq.ft. (%)	
Port Alberni, B.C.	183	115
Vancouver, B.C.	174	83
Pine Hill, Ala.	133	136
Nipigon, Ont.	26	23
	516	357

Waterboard		
Hudson Bay, Sask.	150	135
Thunder Bay, Ont.	128	124
	278	259

Particleboard		
Vancouver, B.C.	108	82

Sales of Raw Materials and Building Materials Products (\$ millions)

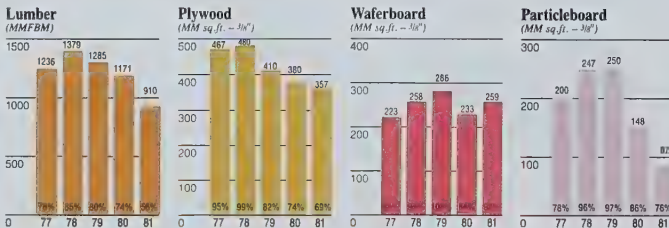
	1977	1978	1979	1980	1981
Lumber	\$ 488.7	\$ 621.5	\$ 734.7	\$ 705.3	\$ 534.3
Plywood	104.4	124.4	123.1	111.8	121.7
Waferboard	54.2	60.9	63.0	58.4	60.6
Particleboard	14.5	29.9	30.6	29.3	16.7
Other (includes inter-segment sales of logs and chips)	199.1	195.0	225.1	251.9	213.6
Total Segment Sales	\$ 860.9	\$1,031.7	\$1,176.5	\$1,156.7	\$ 946.9
Segment Contribution to Operating Earnings	\$ 29.4	\$ 92.1	\$ 155.4	\$ 56.9	\$ (82.2)

Building Materials Sales by Market in 1981*

	Lumber MMFBM	Plywood MM sq.ft. (%)*	Waferboard MM sq.ft. (%)*
British Columbia	138	46	11
Rest of Canada	105	149	170
United States	597	211	168
Japan and Orient	193	—	—
United Kingdom and Europe	163	75	1
Other	120	1	—
Total	1,316	482	350

*Includes products not produced by MacMillan Bloedel.

Building Materials Production



Percentage figures are average annual operating rates

Building Materials Sales Offices and Distribution Centres

Canada: MacMillan Bloedel Building Materials, Dartmouth, N.S. • Moncton, N.B. • Montreal, Que. • Noranda, Que. • Quebec City, Que. • Rimouski, Que. • Fonthill, Ont. • Kitchener, Ont. • London, Ont. • Orillia, Ont. • Ottawa, Ont. • Sault Ste. Marie, Ont. • Sudbury, Ont. • Thunder Bay, Ont. • Timmins, Ont. • Toronto, Ont. • Winnipeg, Man. • Regina, Sask. • Saskatoon, Sask. • Calgary, Alta. • Edmonton, Alta. • Lethbridge, Alta. • Port Alberni, B.C. • Vancouver, B.C.

United States: MacMillan Bloedel Building Materials, Walpole, MA • Brooklyn, NY • Camden, NJ • Ashtabula, OH • Baltimore, MD • Fort Lauderdale, FL • Jacksonville, FL • Los Angeles, CA • Tampa, FL • West Hartford, CT • Atlanta, GA • Dallas, TX • Houston, TX • Portland, OR

United Kingdom: MacMillan Bloedel Meyer Limited, London • MacMillan Bloedel Panelboard Agencies Limited, London

Australia: MacMillan Bloedel Pty. Limited, Sydney

Orient: MacMillan Jardine Limited, Hong Kong • Japan

Other Wood Products Facilities:

Port Alberni, B.C. (Shakes and Shingles) • Sturgeon Falls, Ont. (Hardboard Siding) • Toronto, Ont. (Mouldings) • Vancouver, B.C. (Pres-to-logs and Panelboard Specialties) • New Westminster, B.C. (Wood Preserving and Pole Manufacturing)

Woodlands Divisions B.C.

Cameron • Chemainus • Estevan • Eve River • Franklin River • Hecate • Kelsey Bay • Kennedy Lake • Menzies Bay • Northwest Bay • Port McNeill • Queen Charlotte • Sarita • Shawnigan • Sproat Lake • Squamish • Stillwater

Present Productive Assets

Historical cost and current cost of acquiring new assets of equivalent productive capacity (Notes 1 and 2)

	December 31			
	1981 Replacement Basis	Historical Basis	1980 Replacement Basis	Historical Basis
(\$ millions)				
Buildings and Equipment:				
Cost	\$5,524.6	\$1,904.5	\$5,143.2	\$1,742.7
Accumulated depreciation	2,915.2	785.5	2,624.4	764.2
Net	\$2,609.4	\$1,119.0	\$2,518.8	\$ 978.5
Depreciation for year	\$ 223.9	\$ 74.1	\$ 211.4	\$ 71.8

Effect of Inflation on Funds Available to Maintain Present Productive Capacity (Note 2)

	Year ended December 31	
	1981	1980
(\$ millions)		
Funds generated from operations (as shown in the statements of changes in financial position)	\$ 32.8	\$245.9
Funds required to finance replacement of productive capacity if no inflationary cost increases had occurred (historical cost depreciation)	74.1	71.8
	(41.3)	174.1
Additional funds required to finance the inflationary increase in the cost of maintaining present productive capacity		
Inventories (Note 3)	59.4	54.7
Buildings and equipment (Notes 1 and 4)	149.8	139.6
	209.2	194.3
Deficiency in funds (Note 5)	\$(250.5)	\$ (20.2)

Notes:

1. The replacement information is based on the hypothetical assumption that MacMillan Bloedel would replace its productive capacity at December 31. Actual decisions concerning replacements will be made with due consideration for economic, regulatory, competitive and technological conditions existing at the time of such determination which could differ materially from the assumptions on which the data are based. The replacement cost of buildings and equipment is based on engineering estimates compiled in 1976 updated to reflect current costs.
2. The replacement cost of timber, land and logging roads has not been taken into account. In the case of timber it is not practicable to estimate a replacement cost owing to the complex nature of the agreements relating to the timber supply. Land has not been taken into account as it is not consumed in the production process. Under existing timber harvesting practices, active logging roads are considered as not requiring replacement beyond annual maintenance until the next timber growth cycle is complete.

3. The increased cost of replacing inventories represents the difference between the historical cost and the current cost of goods sold at the date of sale.
4. The increased cost of maintaining the present productive capacity represents the difference between depreciation determined on an historical cost basis and that determined on the replacement cost of buildings and equipment.
5. No allowance has been made for improvements in operating cash flows which could result from the replacement of productive capacity based on new technology, economies of scale and other similar factors.

Impact of Inflation

Historical Summary

Earnings (\$ millions)	1981	1980	1979	1978
Sales and other income	\$2,230.1	\$2,456.2	\$2,204.6	\$2,010.4
Cost of sales and services	2,013.0	2,062.8	1,770.6	1,662.1
Selling, general and administrative expense	203.8	181.3	148.0	144.7
Interest expense	63.2	31.9	28.9	32.7
Income taxes	(31.3)	63.0	100.4	77.5
Equity in earnings (losses) of partly-owned companies	(3.9)	—	1.8	9.4
Minority interests in subsidiaries	(4.2)	(4.0)	(3.6)	(1.9)
Extraordinary items	30.0	—	—	—
Net earnings (loss)	\$ 3.3	\$ 113.2	\$ 154.9	\$ 100.9
Changes in Financial Position (\$ millions)				
Sources				
Net earnings (loss)	\$ 3.3	\$ 113.2	\$ 154.9	\$ 100.9
Non-cash charges, etc.	29.5	132.7	102.7	99.7
Cash flow from operations	32.8	245.9	257.6	200.6
Long term financing	160.1	296.2	4.6	56.2
Other, including disposition of non-current assets	89.0	34.9	108.5	9.4
Total Sources	281.9	577.0	370.7	266.2
Applications				
Plant and equipment	283.4	306.5	255.1	105.5
Timber and land	24.5	21.2	25.3	16.1
Dividends to shareholders of the Company – Preferred	14.1	5.9	5.4	3.9
– Common	24.6	37.2	37.2	20.2
Other	43.8	104.5	28.7	112.5
Total Applications	390.4	475.3	351.7	258.2
Increase (decrease) in working capital	\$ (108.5)	\$ 101.7	\$ 19.0	\$ 8.0
Balance Sheet (selected items) (\$ millions)				
Property, plant and equipment (net book value)	\$1,266.3	\$1,121.0	\$ 899.2	\$ 710.5
Long term debt	596.8	550.8	323.1	341.7
Share capital – Preferred	211.9	138.0	88.0	88.0
– Common	177.2	171.5	171.5	171.2
Retained earnings	575.5	611.9	542.9	430.6
Other				
Return on invested capital (1)	.1 %	12.0%	16.0%	11.6%
Return on Common shareholders' equity (3)	(1.5)%	14.3%	22.8%	17.0%
Invested capital at year end (millions) (2)	\$1,889.9	\$1,802.0	\$1,360.8	\$1,267.3
Net earnings as a percentage of sales and other income	.1%	4.6%	7.0%	5.0%
Debt as a percentage of invested capital (4)	38.3%	35.0%	26.6%	32.5%
Net earnings (loss) per Common share				
Before extraordinary items (dollars)	\$ (1.94)	\$ 5.03	\$ 7.03	\$ 4.50
After extraordinary items (dollars)	\$ (.53)	\$ 5.03	\$ 7.03	\$ 4.50
Operating cash flow per Common share (dollars)	\$ 1.54	\$ 11.56	\$ 12.11	\$ 9.43
Common shares outstanding at year end (millions)	21.42	21.27	21.27	21.26
Dividends per Common share (dollars)	\$ 1.15	\$ 1.75	\$ 1.75	\$.95
Book value per Common share (dollars)	\$ 35.05	\$ 36.76	\$ 33.54	\$ 28.26
Price range of Common shares – High (dollars)	\$ 53.38	\$ 43.25	\$ 30.00	\$ 25.37
– Low (dollars)	\$ 20.00	\$ 24.25	\$ 20.50	\$ 15.50

1977	1976	1975	1974	1973	1972	1971
\$1,714.8	\$1,523.3	\$1,297.5	\$1,398.8	\$1,219.2	\$ 966.5	\$ 778.0
1,443.1	1,315.9	1,174.0	1,171.6	992.9	827.8	673.9
125.8	114.5	110.6	92.8	66.7	55.1	47.3
32.3	33.7	31.7	21.4	15.1	17.2	18.8
54.1	36.1	(2.8)	58.1	66.6	32.5	20.1
3.2	1.2	(3.1)	19.1	6.2	4.0	1.6
(2.0)	(1.5)	.2	(1.7)	(2.3)	(.3)	3.0
(22.3)	—	—	—	—	2.6	3.4
\$ 38.4	\$ 22.8	\$ (18.9)	\$ 72.3	\$ 81.8	\$ 40.2	\$ 25.9
\$ 38.4	\$ 22.8	\$ (18.9)	\$ 72.3	\$ 81.8	\$ 40.2	\$ 25.9
98.7	79.6	80.8	59.3	60.0	50.7	42.0
137.1	102.4	61.9	131.6	141.8	90.9	67.9
102.6	41.0	47.2	77.0	3.9	.9	30.0
17.4	11.9	26.4	14.2	15.8	36.5	15.5
257.1	155.3	135.5	222.8	161.5	128.3	113.4
67.1	64.8	78.0	135.4	84.0	57.9	34.6
10.3	4.5	4.0	12.3	5.5	5.6	3.3
3.7	—	—	—	—	.1	.1
8.5	7.4	13.9	37.1	26.3	20.8	10.4
112.0	29.1	35.8	35.3	26.2	19.0	21.6
201.6	105.8	131.7	220.1	142.0	103.4	70.0
\$ 55.5	\$ 49.5	\$ 3.8	\$ 2.7	\$ 19.5	\$ 24.9	\$ 43.4
\$ 669.9	\$ 670.5	\$ 674.6	\$ 659.5	\$ 584.9	\$ 553.6	\$ 542.6
309.8	372.8	346.9	316.3	251.7	263.2	273.8
88.0	—	—	—	—	.6	2.6
171.2	171.2	171.2	170.2	169.3	160.0	160.0
353.8	327.6	312.2	343.3	302.9	247.4	228.1
7.8%	4.0%	.5%	10.5%	11.8%	5.8%	3.2%
6.8%	4.7%	(3.8)%	14.7%	18.6%	10.1%	6.8%
\$1,140.1	\$1,087.8	\$1,040.4	\$1,050.0	\$ 864.1	\$ 801.0	\$ 795.1
2.2%	1.5%	(1.5)%	5.2%	6.7%	4.2%	3.3%
34.0%	39.6%	39.0%	38.1%	31.1%	34.7%	40.8%
\$ 2.70	\$ 1.07	\$ (.89)	\$ 3.41	\$ 3.90	\$ 1.80	\$ 1.08
\$ 1.65	\$ 1.07	\$ (.89)	\$ 3.41	\$ 3.90	\$ 1.92	\$ 1.24
\$ 6.44	\$ 4.81	\$ 2.92	\$ 6.20	\$ 6.77	\$ 4.36	\$ 3.25
21.26	21.26	21.26	21.22	21.19	20.88	20.88
\$.40	\$.35	\$.65	\$ 1.75	\$ 1.25	\$ 1.00	\$.50
\$ 24.69	\$ 23.46	\$ 22.74	\$ 24.20	\$ 22.28	\$ 19.51	\$ 18.59
\$ 24.75	\$ 24.00	\$ 25.75	\$ 33.25	\$ 40.00	\$ 28.50	\$ 28.37
\$ 16.00	\$ 17.75	\$ 16.75	\$ 20.25	\$ 25.37	\$ 22.62	\$ 19.75

Definitions:

- Return on invested capital is defined as Net Operating Profit After Taxes (NOPAT) as a percentage of average invested capital. NOPAT is the sum of:
 - net earnings before extraordinary items and minority interests
 - the change in deferred income taxes
 - interest expense net of associated current taxes
- Invested capital is defined as the sum of:
 - interest-bearing debt (short term and long term)
 - deferred income taxes
 - minority interests
 - preferred share capital
 - common shareholders' equity including retained earnings
- Return on Common shareholders' equity is defined as net earnings available to Common shareholders as a percentage of average Common shareholders' equity.
- Debt is defined to include all long and short term interest-bearing debt, capitalized leases and term preferred shares within five years of maturity.

Directors and Officers

Committees of the Board

- Executive Committee ■
- Audit Committee ■
- Compensation Committee ■
- Nominating Committee ■
- Pension Fund Investment ■
- Advisory Committee ■
- Donations Committee ■

Directors

- E. K. Cork** ■ ■
Toronto, Ontario
Senior Vice-President, Treasurer
Noranda Mines Limited
- D. M. Culver** ■ ■
Montreal, Quebec
President and Chief Executive Officer
Alcan Aluminium Limited
- D. C. Davenport** ■ ■
Vancouver, British Columbia
Partner, Bourne, Lyall,
Davenport & Herbert
- J. P. Fisher** ■
Edmonton, New Brunswick
President, Fraser Inc.
- R. E. Harrison** ■ ■
Toronto, Ontario
Chairman and Chief Executive Officer
Canadian Imperial Bank of Commerce
- G. H. D. Hobbs** ■ ■ ■ ■
Vancouver, British Columbia
Corporate Director
- J. N. Hyland** ■ ■ ■ ■ ■
Vancouver, British Columbia
Corporate Director
- C. C. Knudsen** ■ ■ ■
Vancouver, British Columbia
Chairman and Chief Executive Officer
MacMillan Bloedel Limited
- A. Powis** ■ ■
Toronto, Ontario
Chairman and President
Noranda Mines Limited
- R. V. Smith** ■ ■ ■
Vancouver, British Columbia
President and Chief Operating Officer
MacMillan Bloedel Limited
- Jean M. Southam** ■ ■
Vancouver, British Columbia
Private Investor
- The Honourable J. N. Turner,**
P.C., Q.C. ■
Toronto, Ontario
Partner, McMillan Binch

- C. B. Wright** ■ ■ ■ ■
Seattle, Washington
Private Investor
- A. H. Zimmerman** ■ ■ ■ ■
Toronto, Ontario
Executive Vice-President
Noranda Mines Limited

Officers

- C. C. Knudsen**
Chairman and Chief Executive Officer
- A. H. Zimmerman**
Vice-Chairman of the Board
- R. V. Smith**
President and Chief Operating Officer
- R. B. Findlay**
Senior Vice-President, Alberni Region
- O. L. Forgacs**
Senior Vice-President,
Research and Development
- S. W. Forstrom**
Senior Vice-President, Powell River Region
- J. L. Howard**
Senior Vice-President,
Law and Corporate Affairs
- J. H. Lawson**
Senior Vice-President,
Raw Materials Services
- D. L. McLaughlin**
Senior Vice-President,
Containerboard and Packaging Group
- Wilhelm Peppler**
Senior Vice-President, International
- J. S. Rogers**
Senior Vice-President, Engineering
- J. St. C. Ross**
Senior Vice-President, Nanaimo Region
- G. J. Towill**
Senior Vice-President, Human Resources
- R. N. Wiewel**
Senior Vice-President, Marketing Group
- G. L. Ainscough**
Vice-President and Chief Forester
- J. C. Bauer**
President, MacMillan Bloedel
Containers (U.S.)
- J. D. Bence**
Managing Director, MacMillan Bloedel
Containers (U.K.)
- J. G. Dickinson**
Vice-President, Planning and Analysis
- D. A. Dowsley**
Vice-President, Building Materials,
Nanaimo Region
- J. M. Fletcher**
Treasurer
- D. H. Holden**
Vice-President, Corporate Communications
- Claire-Marie Jadot**
Assistant Secretary
- G. H. Johncox**
Vice-President, Industrial Relations
- E. Lauritzen**
Vice-President,
Pulp and Paper, Marketing Group
- E. G. Legg**
Vice-President, Controller, Marketing
Group
- R. D. MacFayden**
Secretary
- R. V. Matthews**
Corporate Controller
- F. H. Moonen**
Vice-President, Government Affairs
- W. W. Shorter**
President, MacMillan Bloedel Inc.
- W. L. Stapleton**
Vice-President,
Information Systems & Services
- D. W. St. John**
Vice-President, Lumber, Marketing Group
- G. M. Wilson**
Vice-President, Finance
- V. R. Worthly**
Vice-President, Panelboards,
Marketing Group

Exchange Listings

Common Share Listings:

New York, Toronto, Montreal,
Vancouver

Class B Convertible Preferred Share Listings:

Toronto, Montreal, Vancouver

Ticker Symbols

New York Stock Exchange: MMB

Canadian Stock Exchanges: MB

Transfer Agents and Registrars

The Canada Trust Company

Transfer Agent

Vancouver, Calgary, Regina, Winnipeg,
Toronto, Montreal, St. John (through its
agent the Canada Permanent Trust
Company)

The Royal Trust Company

Registrar

Vancouver, Calgary, Regina, Winnipeg,
Toronto, Montreal, St. John

The Chase Manhattan Bank

Transfer Agent and Registrar

New York

Tax Provisions Relating to Dividends and Interest to Non-Resident Security Holders

Under the Canada-United States Tax Convention, dividends paid to United States shareholders of the Company's shares are subject to a 15% Canadian non-resident withholding tax. Also under that Convention, interest paid to United States holders of the Company's debt obligations is subject to 15% Canadian non-resident withholding tax, except interest payable to holders of bonds issued by the Company after June 23, 1975 where the terms of the bonds do not require repayment of more than 25% of the principal amount of the issue within five years from the date of issue.

Form 10-K Available

The Company's Annual Report to the United States Securities and Exchange Commission (Form 10-K) is available on request. Write to:

*The Secretary,
MacMillan Bloedel Limited
1075 West Georgia Street
Vancouver, B.C. V6E 3R9*

Geographic Distribution of Common Shares and Common Shareholders as at February 10, 1982

	Common Shares	Common Shareholders
Canada	20,085,492	9,344
United States	1,305,974	805
Other	27,541	113
	21,419,007	10,262
Share Warrants	186	
	21,419,193	

Shareholder Information

Cover stock:

Manufactured by MacMillan Bloedel's
affiliate, Koninklijke Nederlandse
Papierfabrieken N.V., Maastricht, Holland.

Text stock:

Manufactured by MacMillan Bloedel's
Island Paper Mills Division, New
Westminster, B.C.

